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2528  
**No. 11909**

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**United States**  
**Circuit Court of Appeals**

**For the Ninth Circuit.**

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**HAWAIIAN TRUST COMPANY, LIMITED,**  
Executor of the Will of Laura D. Sherman,  
Appellant,  
vs.

**AGNES M. KANNE, Executrix under the Will of**  
**Fred H. Kanne, Deceased,**  
Appellee.

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**Transcript of Record**

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**Upon Appeal from the District Court of the United States**  
**for the Territory of Hawaii**

**FILED**

**JUN 24 1948**

**PAUL P. O'BRIEN,**

**CLERK**





No. 11909

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United States  
Circuit Court of Appeals  
For the Ninth Circuit.

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HAWAIIAN TRUST COMPANY, LIMITED,  
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Transcript of Record

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Upon Appeal from the District Court of the United States  
for the Territory of Hawaii

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# INDEX

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

	PAGE
Answer .....	31
Appeal:	
Bond for Costs on.....	55
Certificate of Clerk to Transcript of Record on.....	64
Designation (DC) of Record on.....	59
Notice of.....	55
Statement of Points and Designation (CCA) on.....	77
Statement of Points (DC) Relied Upon on	60
Stipulation re Record on.....	62
Bond for Costs on Appeal.....	55
Certificate of Clerk, U. S. District Court, to Transcript of Record on Appeal.....	64
Clerk's Statement.....	2
Certificate of Clerk to the Above Statement	3
Complaint .....	4
Exhibit A—Agreement Between G. Sherman and Laura D. Sherman	
Dated 12/26/35.....	11
B—Assignment Dated 4/28/36....	19
C—Assignment Dated 4/16/36....	21
D—Assignment Dated 4/16/36....	23
E—Income Tax Claim for Refund	
1/1/40-12/31/40 .....	27
F—Income Tax Claim for Refund	
1/1/41-12/31/41 .....	28

Designation of Record on Appeal (DC).....	59
Exhibits for Defendant:	
No. 1—Certificate of Assessments and Pay- ments .....	76
Exhibits for Plaintiff:	
A—Decree of Divorce.....	65
B—Supplementary Stipulation.....	68
Judgment of Dismissal.....	52
Minutes of Court.....	53
Motion to Substitute Executor as Plaintiff With Consent of Defendant.....	36
Motion to Substitute Executrix as Defendant With Consent of Executrix.....	34
Names and Addresses of Attorneys of Record.	1
Notice of Appeal.....	55
Order Extending Time to File and Docket Rec- ords With the United States Circuit Court of Appeals for the Ninth Circuit.....	62
Return on Summons.....	29
Special Findings of Fact and Conclusions of Law .....	41
Conclusions of Law.....	50
Special Findings of Fact.....	41
Statement of Points Relied Upon on Appeal (DC) .....	60
Statement of Points (CCA) to Be Relied Upon and Designation of the Record to Be Printed	77
Stipulation of Facts.....	38
Stipulation re Record on Appeal.....	62
Summons .....	29



NAMES AND ADDRESSES OF ATTORNEYS  
OF RECORD

For the Plaintiff, Hawaiian Trust Company,  
Limited:

ANDERSON, WRENN & JENKS,  
By JAMES M. RICHMOND,  
Bank of Hawaii Building,  
Honolulu, T. H.

For the Defendant, Agnes M. Kanne, etc.:

LELAND T. ATHERTON,  
Special Assistant to the Attorney General  
of the United States,  
Washington, D. C.

UNITED STATES DISTRICT ATTORNEY,  
By EDWARD A. TOWSE,  
Assistant United States District Attorney,  
Federal Building,  
Honolulu, T. H. [2\*]

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\*Page numbering appearing at foot of page of original certified Transcript of Record.

In the United States District Court for the  
District of Hawaii

Civil No. 619

HAWAIIAN TRUST COMPANY, LIMITED,  
Executor of the Will of Laura D. Sherman,  
Plaintiff,

vs.

AGNES M. KANNE, Executrix Under the Will  
of Fred H. Kanne, Deceased,  
Defendant.

### CLERK'S STATEMENT

Time of Commencing Suit:

October 30, 1945 — Complaint with Exhibits  
Filed

Names of Original Parties:

Laura D. Sherman, Plaintiff  
Fred H. Kanne, Defendant

Dates of Filing Pleadings:

February 27, 1946—Answer

March 25, 1947—Motion to Substitute Execu-  
trix as Defendant with Consent of Executrix

July 22, 1947—Motion to Substitute Executor  
as Plaintiff with Consent of Defendant

September 24, 1947—Stipulation of Facts

November 21, 1947—Special Findings of Fact  
and Conclusions of Law

February 17, 1948—Judgment of Dismissal

Times When Proceedings Were Had:

November 10, 1947—Trial [3]

Proceedings in the above-entitled matter were had before the Honorable D. E. Metzger, Judge, United States District Court, District of Hawaii.

Dates of Filing Appeal Documents:

March 17, 1948—Notice of Appeal

Bond for Costs on Appeal

March 29, 1948—Statement of Points Relied Upon on Appeal

Designation of Record on Appeal

April 5, 1948—Order Extending Time to File and Docket Records with the United States Circuit Court of Appeals for the Ninth Circuit

CERTIFICATE OF CLERK TO THE  
ABOVE STATEMENT

United States of America,  
District of Hawaii—ss.

I, Wm. F. Thompson, Jr., Clerk of the United States District Court for the District of Hawaii, do hereby certify the foregoing to be a full, true and correct statement showing the time of commencement of the above-entitled cause, the names of the original parties, the dates when the respective pleadings were filed, the times when proceedings were had, the name of the judge presiding, and the dates when appeal pleadings were filed in the above-entitled cause.



In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court this 19th day of April, 1948.

[Seal]      /s/ WM. F. THOMPSON, JR.,  
Clerk, United States District  
Court, District of Hawaii.

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In the United States District Court for the  
Territory of Hawaii

Civil No. 619

LAURA D. SHERMAN,

Plaintiff,

vs.

FRED H. KANNE, Collector of Internal Revenue  
of the United States for the District of Hawaii,  
Defendant.

### COMPLAINT

Laura D. Sherman, a resident of the Territory of Hawaii, brings this action against the defendant, Fred H. Kanne, Collector of Internal Revenue of the United States for the District of Hawaii, and complains and alleges as follows:

#### I.

The grounds upon which the jurisdiction of this Court depends are:

1. This is a civil action by a citizen of the Territory of Hawaii against a Collector of Internal

Revenue of the United States for the recovery of income taxes illegally assessed and collected and arises under the act of March 2, 1929, Chapter 488, Section 1, 45 Stat. 1475; U.S.C., title 28, sec. 41 (5), as hereinafter more fully appears.

2. The plaintiff has complied with the requirements of section 3772 (a) (1) and (2) of the Internal Revenue Code regarding the filing of claim for refund with the Commissioner of Internal Revenue, as hereinafter more fully appears. [6]
3. Defendant Fred H. Kanne is now and at all times since on or about August 1, 1933, has been Collector of Internal Revenue of the United States for the District of Hawaii and is a resident of said Hawaii, and that plaintiff claims of defendant the sum of \$2,404.46 with interest as provided by law, representing income taxes illegally exacted from plaintiff by defendant as hereinafter more fully appears.

## II.

On December 26, 1935, George Sherman, husband of the plaintiff, entered into an agreement with the plaintiff and Hawaiian Trust Company, Limited, a Hawaiian corporation, a true copy of which agreement is annexed hereto, marked Exhibit "A" and hereby made a part hereof. Said agreement created an irrevocable trust of which Hawaiian Trust Company, Limited, and plaintiff were and are trustees and provided that all of the net income derived

from the trust estate be paid to plaintiff during her lifetime.

### III.

Frederick Dickson Nott, son of the plaintiff, was divorced from Anna Adams Nott by a decree of final divorce on April 28, 1936, in action numbered Divorce 16861 in the files of the Clerk of the Circuit Court of the First Judicial Circuit, Territory of Hawaii. The decree directed said Frederick Dickson Nott to pay alimony of \$100 per month to the divorced wife and in addition to pay her \$75 per month each for the support and maintenance of Frederick Dickson K. Nott and Gretchen K. Nott, minor children of the Notts, whose custody was awarded to said Anna Adams Nott. [7]

### IV.

By three separate instruments, each dated April 16, 1936, the plaintiff made assignments of her right to receive income from said trust estate in the amounts of \$100 per month to Anna Adams Nott until her death or remarriage, whichever should first occur, and \$75 per month each to said Anna Adams Nott for the support of each of said Frederick Dickson K. Nott and Gretchen K. Nott until the respective child's death or majority, whichever should first occur. True copies of said assignments are attached hereto, marked repectively Exhibits "B," "C" and "D," and are hereby made a part hereof. These assignments were made because said Frederick Dickson Nott did not have sufficient income to enable him to pay the amounts



to be ordered in the divorce decree and because the plaintiff desired to assist him financially. Said Frederick Dickson K. Nott and Gretchen K. Nott were ten and nine years of age, respectively, at the time of said assignments.

#### V.

The said assignments were assignments of beneficial interests in and to the corpus of said trust estate and the assignees thereby became owners of the said beneficial interests, which during the taxable years in question produced income of \$3,000.00 per annum. The plaintiff by said assignment effected a transfer of income-bearing property to and for the benefit of the assignees and the income thereafter received therefrom is the income of the assignees and not that of the plaintiff. [8]

#### VI.

During the calendar year 1940 the distributable share of plaintiff in the income of said trust estate and the amount actually received by her was \$6,332.40. During the calendar year 1941 the distributable share of plaintiff in the income of said trust estate and the amount actually received by her was \$7,598.98. During each of the said years the distributable share of the assignees in the income of said trust estate and the amount actually received by them was \$3,000.00.

#### VII.

The trustees' fiduciary income tax returns for the said trust estate for the years 1940 and 1941

inadvertently showed the plaintiff's distributive share of income to include the \$3,000.00 of income which had been assigned and distributed to the assignees. Because of this inadvertent error plaintiff's distributive shares of income from said trust estate were shown to have been \$9,332.40 and \$10,598.98 for the respective calendar years 1940 and 1941. The plaintiff also inadvertently returned the same amounts as received by her from said trust estate for the years 1940 and 1941. Plaintiff paid income taxes for the year 1940 in the amount of \$4,096.50 to the defendant. Said taxes were paid in equal quarterly instalments on March 15, June 15, September 15 and December 15, 1941. Plaintiff paid income taxes for the year 1941 in the amount of \$6,046.15 to the defendant. Said taxes were paid in equal quarterly instalments on March 15, June 15, September 15 and December 15, 1942. [9]

#### VIII.

The correct amount of plaintiff's income tax for the year 1940 was \$3,126.85 if the amount of income of said trust estate taxable to the plaintiff during 1940 was \$6,332.40. The correct amount of plaintiff's income tax for the year 1940 was \$4,096.50 if the amount of income of said trust estate taxable to the plaintiff during 1940 was \$9,332.40. The correct amount of plaintiff's income tax for the year 1941 was \$4,611.34 if the amount of income of said trust estate taxable to the plaintiff during 1941 was \$7,598.98. The correct amount of plaintiff's income tax for the year 1941 was \$6,046.15

if the amount of income of said trust estate taxable to the plaintiff during 1941 was \$10,598.98.

### IX.

The correct income tax liabilities of plaintiff to the United States of America for the years 1940 and 1941 were \$3,126.85 and \$4,611.34, respectively. Amounts in excess thereof equalling \$969.65 and \$1,434.81 for the years 1940 and 1941, respectively, have been illegally assessed and collected by the defendant and should be returned to the plaintiff. Said amounts were so assessed and collected on the basis that the said \$3,000.00 distributed by the said trustees to the assignees for each of the years 1940 and 1941 was income taxable to the plaintiff.

### X.

On March 14, 1944, plaintiff filed with the Commissioner of Internal Revenue a claim for refund of said \$969.65 of 1940 [10] income taxes and a claim for refund of said \$1,434.81 of 1941 income taxes. True copies of said claims are attached hereto, marked respectively Exhibits "E" and "F," and hereby made a part hereof. No action has been taken by said Commissioner on either of said claims for a period in excess of six months from the time of filing said claims with him. Said claims have been disallowed by the said Commissioner.

### XI.

No amount has been paid to the plaintiff on account of said total sum of \$2,404.46 claimed as in-



come tax and so illegally assessed and collected by the defendant from the plaintiff.

## XII.

Plaintiff is entitled to receive from defendant the said sum of \$2,404.46, together with interest on \$969.65 from December 15, 1941, and interest on \$1,434.81 thereof from December 15, 1942, until the same is paid. Plaintiff has observed and performed the provisions and requirements of the laws of the United States and the rules and regulations prescribed by the Commissioner of Internal Revenue and approved by the Secretary of the Treasury of the United States, and all other matters and things necessary or required to be observed and performed on her part to entitle her to recover the same.

Wherefore, plaintiff prays judgment against defendant in the sum of \$2,404.46, plus interest, as is in such cases [11] provided by section 3773, Internal Revenue Code; U.S.C., title 28, sec. 284, and the costs of such suit and that process issue out of this court requiring defendant to appear and answer this complaint.

Dated at Honolulu, Hawaii, October 26, 1945.

/s/ JAMES M. RICHMOND,

Bank of Hawaii Building,  
Honolulu, Hawaii,

Attorney for Plaintiff.

Of Counsel:

ANDERSON, WRENN & JENKS,

Bank of Hawaii Building,  
Honolulu, Hawaii.

Territory of Hawaii,  
City and County of Honolulu—ss.

Laura D. Sherman, being first duly sworn, on oath deposes and says: That she is the plaintiff in the above entitled action, that she has read the foregoing complaint and knows the contents thereof and that the same are true of her own knowledge.

/s/ LAURA D. SHERMAN

Subscribed and sworn to before me this 26th day of October, 1945.

[Seal] /s/ ALLEN R. MOORE,  
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1949.

[Endorsed]: Filed Oct. 30, 1945. [12]

### EXHIBIT "A"

(Copy)

This Agreement made this 26th day of December, 1935, by and between George Sherman, of Honolulu, Territory of Hawaii, hereinafter called the Settlor, party of the first part, and Laura D. Sherman, of said Honolulu, and Hawaiian Trust Company, Limited, a Hawaiian corporation having its principal office in said Honolulu, hereinafter called the Trustees, parties of the second part,

Witnesseth:

That the Settlor for and in consideration of the execution hereof by the Trustees and of love and affection for the beneficiaries hereinafter named, does hereby assign, transfer, convey and deliver to

the Trustees all of the following shares of corporation capital stock:

- 6700 shares of the common capital stock of American Factors, Limited;
- 875 shares of the common capital stock of Bishop National Bank of Hawaii at Honolulu;
- 500 shares of the common capital stock of Bishop Trust Company, Limited;
- 250 shares of the preferred capital stock of Bishop Trust Company, Limited.

To Have and to Hold the same unto the Trustees and their successors in trust and assigns, in trust, upon the following trusts:

1. The Trustees shall pay to Laura D. Sherman, wife of the Settlor, during the remainder of her life all of the net income derived from said trust estate.

2. Upon the death of said Laura D. Sherman, Hawaiian Trust Company, Limited, as remaining Trustee, shall divide said trust estate into two equal parts, referred to hereinafter as "trust estate A" and "trust estate B," the said division and the equality of the parts to be determined by said Trustee in its sole discretion [13] and to be binding on all the beneficiaries hereunder;

(a) After the death of said Laura D. Sherman, said remaining Trustee shall pay the net income derived from said trust estate A to the Settlor's stepdaughter, Laura Nott Dowsett, so long as she shall live, and after her death to those who shall be surviving from time to time of her children and their issue, in accordance with their respective needs, without obligation to divide the same equally



or proportionately, until the youngest who shall continue to survive of the now living children of the Settlor's stepdaughter shall reach the age of thirty years or the last survivor of her now living children shall die.

(b) When the Settlor's stepdaughter, Laura Nott Dowsett, shall have died and also either the youngest who shall continue to survive of her now living children shall have reached the age of thirty years or the last survivor of her now living children shall have died, the Trustee shall transfer, convey and deliver, absolutely and free from any trust, the principal of said trust estate A, together with any unpaid income derived therefrom, in equal shares to those who shall be then surviving of the children of the Settlor's stepdaughter and of the issue of any of them who shall be then dead, such issue taking per stirpes by right of representation in each generation, or if none of the children or issue of deceased children of the Settlor's stepdaughter shall be then surviving, in equal shares to those who shall be then surviving of the children of the Settler's stepson, Frederick Dickson Nott, and of the issue of any of them who shall be then dead. such issue taking per stirpes by right of representation in each generation; provided, however, if [14] trust estate B under this trust agreement shall be then in existence, said property shall be added to said trust estate B, to be and become a part thereof and the income therefrom and the principal thereof to be distributed as provided under the terms governing said trust estate B.

(c) After the death of said Laura D. Sherman said remaining Trustee shall pay the net income derived from said trust estate B to the Settlor's stepson, Frederick Dickson Nott, so long as he shall live, and after his death to those who shall be surviving from time to time of his children and their issue, in accordance with their respective needs, without obligation to divide the same equally or proportionately, until the youngest who shall continue to survive of the now living children of the Settlor's stepson shall reach the age of thirty years or the last survivor of his now living children shall die.

(d) When the Settlor's stepson, Frederick Dickson Nott, shall have died and also either the youngest who shall continue to survive of his new living children shall have reached the age of thirty years or the last survivor of his now living children shall have died, the Trustee shall transfer, convey and deliver, absolutely and free from any trust, the principal of said trust estate B, together with any unpaid income derived therefrom, in equal shares to those who shall be then surviving of the children of the Settlor's stepson and of the issue of any of them who shall be then dead, such issue taking per stirpes by right of representation in each generation, or if none of the children or issue of deceased children of the [15] Settlor's stepson shall be then surviving, in equal shares to those who shall be then surviving of the children of the Settlor's stepdaughter, Laura Nott Dowsett, and of the issue of any of them who shall be then dead, such issue

taking per stirpes by right of representation in each generation; provided, however, if trust estate A under this trust agreement shall be then in existence, said property shall be added to said trust estate A, to be and become a part thereof and the income therefrom and the principal thereof to be distributed as provided under the terms governing said trust estate A.

3. The Settlor expressly reserves the right from time to time and at any time during his lifetime to add property to the trust estate by transfer of title to the Trustees and delivery to the Hawaiian Trust Company, Limited, as Trustee, and thereupon such additional property shall become part of the principal of the trust estate as if it had been originally included hereunder.

4. The following provisions shall apply during the life of the Settlor's wife to the trust estate hereby established and shall apply after her death to each of the parts into which said trust estate is to be divided upon her death, to wit: trust estate A and trust estate B, and whenever hereinafter the term "trust estate" is used it shall after the death of the Settlor's wife be taken to mean trust estate A and also trust estate B.

5. The Trustees shall have full power and authority to manage and control the property from time to time included in said trust estate, to sell at public or private sale, to exchange, [16] to borrow, to pledge, and to invest and reinvest. It is expressly provided that the Trustees shall have the right and power to invest any moneys at any



time or from time to time in their hands in common stocks and preferred stocks of corporation organized under the laws of the Territory of Hawaii or elsewhere in the United States of America and shall not be limited by any statute or rule of law to the contrary. The Trustees shall treat all stock dividends and rights to subscribe as principal, and all cash dividends, whether regular or extraordinary, unless paid out of capital, as income. The Settlor expressly declares that the shares of corporation capital stock hereby assigned by him to the Trustees have proved satisfactory investments during a considerable period of time and that he does not wish them sold unless the Trustees in their discretion shall think it clearly advisable because of changing conditions or other special reasons. The Trustees shall not be held liable for any loss to the trust estate resulting from the retention of said stock by them.

6. The Trustees shall not be required to file any accounts in any court but shall annually deliver an account to the Settlor's wife, Laura D. Sherman, so long as she shall live, and after her death to each adult beneficiary and to a parent or a guardian of each minor beneficiary. The Trustees shall not be required to give any bond as Trustees.

7. The Trustees shall not be liable for any error of judgment on their part in administering the trusts created hereby but shall each be liable only for her or its own gross neglect or wilful default.

8. Whenever the Trustees shall be required here-

under to make any payments to a minor, such payments may be made in the [17] discretion of the Trustees to a parent or guardian of said minor or to third parties for the benefit of said minor, on their respective receipts.

9. The Trustees shall be entitled to charge commissions at the rate of five per cent (5%) on the gross income derived from said trust estate, and commissions at the rate of one per cent (1%) on the principal of said trust estate on the final payment of the same either in cash or in kind.

10. Upon the termination of this trust the Trustees shall have full power at their option to assign, transfer and deliver to the person or persons then entitled thereto the property then forming the trust estate, or may convert the same into cash for payment of the net proceeds thereof to said person or persons.

11. While Laura D. Sherman is absent from the Territory of Hawaii or temporarily incapable of acting as Trustee by reason of sickness or otherwise, the Hawaiian Trust Company, Limited, shall have all the powers of the Trustees hereunder, and its certificate as to such absence or incapacity of Laura D. Sherman shall be conclusive.

12. In case said Laura D. Sherman shall die or resign or for any other reason shall cease to act or become incapable of acting as one of said Trustees, then and thereafter Hawaiian Trust Company, Limited, shall become and be the sole Trustee hereunder, with all rights and powers and subject to all

the duties herein given or imposed upon the two Trustees named herein, and title to the trust estate shall vest in said Hawaiian Trust Company, Limited, as such sole Trustee, without a conveyance of any kind from said Laura D. Sherman.

13. The Settlor shall have no right to revoke the trust [18] created hereby or to amend the terms or provisions hereof. The Hawaiian Trust Company, Limited, as Trustee, together with those of the Settlor's said stepdaughter and stepson who are at the time alive and capable of joining in the amendment acting unanimously shall have the right at any time to amend the terms and provisions hereof, provided that no amendment shall authorize or permit the payment or application of any part of the principal or income of the trust estate created hereby to or for the benefit of the Settlor or the payment or application of any part of the principal of the trust estate to or for the benefit of the Settlor's said wife.

14. Said Laura D. Sherman and said Hawaiian Trust Company, Limited, as said Trustees, hereby acknowledge the trusts hereby created and agree to perform the same upon the terms and conditions hereinabove set forth.

In Witness Whereof, the Settlor has set his hand hereunto, and said Laura D. Sherman has set her hand hereunto as Trustee, and said Hawaiian Trust Company, Limited, has caused its corporate name to be signed hereto and its corporate seal to be affixed hereunto by its proper officers, thereunto

duly authorized, as Trustee, all as of the day and year first above written, in triplicate.

/s/ GEORGE SHERMAN,  
Settlor.

/s/ LAURA D. SHERMAN.  
HAWAIIAN TRUST  
COMPANY, LIMITED,

By /s/ A. S. DAVIS,  
Its Vice Pres.

By /s/ U. J. RAINALTER,  
Its Vice Pres. [19]  
Trustees.

EXHIBIT "B"  
(Copy)

Know All Men by These Presents:

Whereas by the terms of a certain decree of divorce made and entered on the 28th day of April, 1936, in an action entitled "Anna Adams Nott, libellant, v. F. Dickson Nott, libellee," said action being numbered 16861 in the files of the Clerk of the Circuit Court of the First Judicial Circuit, Territory of Hawaii, the libellant was granted an absolute decree of divorce from the libellee and the libellee was ordered to pay the sum of One Hundred Dollars (\$100.00) a month as alimony to the libellant, and

Whereas at the present time, the libellee's income is insufficient to enable him to pay the sums required of him to be paid by the terms of said decree, and

Whereas the said libellee is the son of the under-



signed Laura D. Sherman and by reason thereof the undersigned desires to assist him financially:

Now Therefore the premises considered, the undersigned, Laura D. Sherman, hereinafter referred to as the assignor, does hereby assign, transfer and set over unto Anna Adams Nott, hereinafter referred to as the assignee, the sum of One Hundred Dollars (\$100.00) a month from the income to which the assignor now is or shall be entitled to receive as life beneficiary under the terms and provisions of that certain unrecorded trust deed dated December 26, 1935, executed by George Sherman as settlor and the assignor and Hawaiian Trust Company, Limited, an Hawaiian corporation, as trustees, until the death or remarriage of the assignee whichever event shall first occur and upon the occurrence of either of said events this assignment shall become inoperative and shall be of no further force or effect. [20]

The Hawaiian Trust Company, Limited, co-trustee under said trust deed, is hereby empowered and directed to pay from the assignor's income, as aforesaid, the sum of One Hundred Dollars (\$100.00) a month to the said assignee, the first of such payments to be made on the 1st day of May, 1936, and a like sum on the 1st day of each and every month thereafter until the death or remarriage of said assignee, whichever event shall first occur, and upon the occurrence of either of such events of which said Hawaiian Trust Company, Limited shall have strict and exact proof, all payments shall cease and determine.

Dated at Honolulu, T. H., this 16 day of April, 1936.

/s/ LAURA D. SHERMAN. [21]

EXHIBIT "C"

(Copy)

This Agreement made this 16 day of April, 1936, between Laura D. Sherman of Honolulu, City and County of Honolulu, Territory of Hawaii, hereinafter referred to as the assignor, and Anna Adams Nott, likewise of Honolulu, hereinafter referred to as the assignee,

Witnesseth:

Whereas by the terms of a certain decree of divorce made and entered on the 28th day of April, 1936, in an action entitled "Anna Adams Nott, libellant v. F. Dickson Nott, libellee" said action being numbered 16861 in the files of the Clerk of the Circuit Court of the First Judicial Circuit, Territory of Hawaii, custody of Frederick Dickson K. Nott, minor child of the libellant and libellee, was awarded to the libellant and the libellee was ordered to pay to the libellant for the support and maintenance of said minor the sum of Seventy-Five Dollars (\$75.00) a month, and

Whereas, at the present time, the libellee's income is insufficient to enable him to pay the sums required of him to be paid by the terms of said decree, and

Whereas, the said libellee is the son of the assignor and the above mentioned minor is the assignor's grandchild and by reason thereof the

assignor desires to provide for the support, education and maintenance of said minor.

Now Therefore in consideration of the premises and of the promise of the assignee hereinafter contained the assignor does hereby assign, transfer and set over unto the assignee the sum of Seventy-five Dollars (\$75.00) a month from the income to which the assignor now is or shall be entitled to receive as life beneficiary under the terms and provisions of that certain unrecorded trust deed dated December 26, 1935, executed by George Sherman as settlor and the assignor and Hawaiian Trust Company, Limited, an Hawaiian corporation, as trustees, which sum is to be used by the assignee solely for the support, education and maintenance of said minor during his minority provided, however, and this assignment is upon this express condition, that upon the occurrence of any of the following events this assignment shall become inoperative and all payments authorized to be made herein shall cease and determine, such events being:

- (1) Upon the death of said minor or the assignee;
- (2) Upon the said minor attaining his majority under the laws of the jurisdiction in which said minor is then living;

The Hawaiian Trust Company, Limited, co-trustee under said trust deed, is hereby empowered and directed to pay from the assignor's income, as aforesaid, the sum of Seventy-five Dollars (\$75.00) a month to the said assignee, the first of such pay-

ments to be made on the 1st day of May, 1936, and a like sum of the 1st day of each and every month thereafter until the occurrence of any one or more of the above mentioned events and upon the occurrence of any of such events (of which said Hawaiian Trust Company, Limited, shall have strict and exact proof) all payments shall cease and determine. [23]

And the assignee in consideration of the foregoing does covenant and agree with the assignor that she will use such sums as are paid to her hereunder solely for the support, education and maintenance of said minor.

In Witness Whereof the parties hereto have set their hands the day and year first above written.

/s/ LAURA D. SHERMAN,

/s/ ANNA ADAMS NOTT. [24]

### EXHIBIT "D"

(Copy)

This Agreement made this 16 day of April, 1936, between Laura D. Sherman of Honolulu, City and County of Honolulu, Territory of Hawaii, hereinafter referred to as the assignor, and Anna Adams Nott, likewise of Honolulu, hereinafter referred to as the assignee,

Witnesseth:

Whereas by the terms of a certain decree of divorce made and entered on the 28th day of April, 1936, in an action entitled "Anna Adams Nott, libellant v. F. Dickson Nott, libellee" said action being numbered 16861 in the files of the Clerk of



the Circuit Court of the First Judicial Circuit, Territory of Hawaii, custody of Gretchen K. Nott, minor child of the libellant and libellee, was awarded to the libellant and the libellee was ordered to pay to the libellant for the support and maintenance of said minor the sum of Seventy-five Dollars (\$75.00) a month, and

Whereas, at the present time the libellee's income is insufficient to enable him to pay the sums required of him to be paid by the terms of said decree, and

Whereas, the said libellee is the son of the assignor and the above mentioned minor is the assignor's grandchild and by reason thereof the assignor desires to provide for the support, education and maintenance of said minor.

Now Therefore in consideration of the premises and of the promise of the assignee hereinafter contained the assignor does hereby assign, transfer and set over unto the assignee the sum of Seventy-five Dollars (\$75.00) a month from the income to which the assignor now is or shall be entitled to receive as life beneficiary under the terms and provisions [25] of that certain unrecorded trust deed dated December 26, 1935 executed by George Sherman as settlor and the assignor and Hawaiian Trust Company, limited, an Hawaiian corporation as trustees, which sum is to be used by the assignee solely for the support, education and maintenance of said minor during her minority provided, however, and this assignment is upon this express condition, that upon the occurrence of any of the following events

this assignment shall become inoperative and all payments authorized to be made herein shall cease and determine, such events being:

- (1) Upon the death of said minor or the assignee;
- (2) Upon the said minor attaining her majority under the laws of the jurisdiction in which said minor is then living;

The Hawaiian Trust Company, Limited, co-trustee under said trust deed, is hereby empowered and directed to pay from the assignor's income, as aforesaid, the sum of Seventy-five Dollars (\$75.00) a month to the said assignee, the first of such payments to be made on the 1st day of May, 1936, and a like sum on the 1st day of each and every month thereafter until the occurrence of any one or more of the above mentioned events and upon the occurrence of any of such events (of which said Hawaiian Trust Company, Limited, shall have strict and exact proof) all payments shall cease and determine, [26]

And the assignee in consideration of the foregoing does covenant and agree with the assignor that she will use such sums as are paid to her hereunder solely for the support, education and maintenance of said minor.

In Witness Whereof the parties hereto have set their hands the day and year first above written.

/s/ LAURA D. SHERMAN.

/s/ ANNA ADAMS NOTT.



COPY

Form 642  
TREASURY DEPARTMENT  
INTERNAL REVENUE SERVICE  
(Revised April 1940)

# CLAIM

TO BE FILED WITH THE COLLECTOR WHERE ASSESSMENT WAS MADE OR TAX PAID

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

- ☐ REFUND OF TAX ILLEGALLY COLLECTED.
- ☐ REFUND OF AMOUNT PAID FOR STAMPS UNTURNED, OR USED IN ERROR OR EXCESS.
- ☐ ABATEMENT OF TAX ASSESSED (not applicable to estate or income taxes).

COLLECTOR'S STAMP (Date received)
--------------------------------------

STATE OF TERRITORY OF HAWAII  
CITY &  
COUNTY OF HONOLULU

Name of taxpayer or purchaser of stamps LAURA D. SHERMAN

Business address 2 Hawaiian Trust Company, Limited  
(Street) (City) (State)

Residence Honolulu, Hawaii

TYPE  
OR  
PRINT

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

- District in which return (if any) was filed Honolulu, Hawaii
- Period (if for income tax, make separate form for each taxable year) from Jan. 1st, 1940, to Dec. 31st, 1940
- Character of assessment or tax Income Tax
- Amount of assessment, \$ 4096.50; dates of payment 3/15/41; 6/15/41; 9/15/41; 12/15/41
- Date stamps were purchased from the Government
- Amount to be refunded \$ 969.65
- Amount to be abated (not applicable to income or estate taxes) \$ I.R.C.
- The time within which this claim may be legally filed expires, under Section 322(b)(1) of the REVENUE ACT of 1939 on March 15, 1944

The deponent verily believes that this claim should be allowed for the following reasons:

Taxpayer's return for the calendar year 1940 reflected at line 7, income from the George Sherman Living Trust of December 26, 1935 in the sum of \$9,332.40 which amount was in agreement with taxpayer's distributive share of the income of said trust as returned on Fiduciary Form 1041 by Hawaiian Trust Company, Limited as trustee of said trust. Said distributive share as inadvertently overstated on the fiduciary return by the sum of \$3000.00 and therefore also overstated on taxpayer's return for the reason that taxpayer, by irrevocable written assignments providing for the distribution of \$3000.00 of the income of other persons, was only entitled to and actually received \$3000.00 less than the distribution returned by the trustee as payable to taxpayer.

Adjustment of taxpayer's return for the year 1940 to eliminate said \$3000.00 of overstated income would result in a corrected tax liability of \$3,126.85 whereas a tax of \$4,096.50 has been collected, resulting in an overassessment of \$969.65, which should be refunded together with statutory interest.

Sworn to and subscribed before me this

Signed (s) LAURA D. SHERMAN

11th day of March 1944

Notary Public, First Judicial

(s) LOUIS A. WILLS Circuit, Territory of Hawaii

(Signature of officer administering oath)

My commission expires June 30, 1945.

(SEE INSTRUCTIONS ON REVERSE SIDE)

EXHIBIT "E"





COPY

Form 942  
TREASURY DEPARTMENT  
INTERNAL REVENUE SERVICE  
(Revised Jan. 1944)

# CLAIM

TO BE FILED WITH THE COLLECTOR WHERE ASSESSMENT WAS MADE OR TAX PAID

The Collector will indicate in the block below the kind of claim filed, and All in the certificate on the reverse side.

- ☐ REFUND OR TAX ILLEGALLY COLLECTED.
- ☐ REFUND OF AMOUNT PAID FOR STAMPS UNUSED, OR USED IN ERROR OR EXCESS.
- ☐ ABATEMENT OF TAX ASSESSED (not applicable to estate, gift, or income taxes).

COLLECTOR'S STAMP

(Date received)

STATE OF TERRITORY OF HAWAII  
CITY & HONOLULU  
COUNTY OF HONOLULU

Name of taxpayer or purchaser of stamps LAURA D. SHERMAN

Business address % HAWAIIAN TRUST CO., LTD., HONOLULU, T. H.  
(Street) (City)

Residence HONOLULU, HAWAII

TYPE  
OR  
PRINT

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

- District in which return (if any) was filed Honolulu, Hawaii
- Period (if for income tax, make separate form for each taxable year) from Jan. 1st, 1941, to Dec. 31st, 1941
- Character of assessment or tax Income tax
- Amount of assessment, \$6046.15; dates of payment 3/15/42; 6/15/42; 9/15/42; 12/15/42
- Date stamps were purchased from the Government
- Amount to be refunded \$1434.81
- Amount to be abated (not applicable to income, gift, or estate taxes) (b)(1) \$
- The time within which this claim may be legally filed expires, under section 333 of I.R.C. of 1939 (Revenue Act or Internal Revenue Code) on March 15, 1945

The deponent verily believes that this claim should be allowed for the following reasons:

Taxpayer's return for calendar year 1941 reflected at line 9, income from George Sherman Living Trust of December 26, 1935 in the sum of \$10,598.98 which amount was in agreement with taxpayer's distributive share of the income of said trust as returned on Fiduciary Form 1041 by Hawaiian Trust Company, Limited as trustee of said trust. Said distributive share was inadvertently overstated on the fiduciary return by the sum of \$3000.00 and therefore also overstated on taxpayer's return for the reason that taxpayer, by irrevocable written assignments providing for the distribution of \$3000.00 of the income to other persons, was only entitled to and actually received \$3000.00 less than the distribution returned by the trustee as taxable to taxpayer.

Adjustment of taxpayer's return for the year 1941 to eliminate said \$3000.00 of overstated income would result in a corrected tax liability of \$611.34, whereas a tax of \$6,046.15 has been collected, resulting in an overassessment of \$1,434.81, which should be refunded together with statutory interest.

(Attach letter-size sheets if space is not sufficient)

Sworn to and subscribed before me this

Signed (S) LAURA D. SHERMAN

11th day of March, 1944

Notary Public, First Judicial Circuit, Territory of Hawaii

(s) LOUIS A. WILLS

(Signature of officer administering oath)

My commission expires June 30, 1945

(SEE INSTRUCTIONS ON REVERSE SIDE)

29

16-10504-2

EXHIBIT "F"



[Title of District Court and Cause.]

SUMMONS

To the above-named Defendant:

You are hereby summoned and required to serve upon James M. Richmond, Bank of Hawaii Building, Honolulu, Hawaii, plaintiff's attorney, an answer to the complaint which is hereby served upon you, within sixty (60) days after service of this summons upon you, exclusive of the day of service. If you fail to do so, judgment by default will be taken against you for the relief demanded in the complaint.

[Seal]      /s/ WM. F. THOMPSON, JR.

Clerk of Court.

Dated: Honolulu, T. H. October 30th, 1945. [30]

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[Title of District Court and Cause.]

RETURN ON SUMMONS

Territory of Hawaii,

City and County of Honolulu—ss.

George E. Bruns, being first duly sworn on oath deposes and says:

That at all times hereinafter mentioned he has been and now is a Deputy United States Marshal for the Territory of Hawaii;

That on the 30th day of October, 1945, in Honolulu, City and County of Honolulu, Territory of Hawaii, he duly served a certified copy of the Sum-



mons, Complaint and Exhibits A-B-C-D-E and F in the above entitled cause upon Ray J. O'Brien, United States District Attorney, at Honolulu, T. H., and by mailing a certified copy of the said Summons, Complaint and Exhibits A-B-C-D-E and F by registered mail receipt wanted on October 30th, 1945, to Tom C. Clark, Attorney General of the United States of America, Washington, D. C., and further that on November 23rd, 1945, he duly served a certified copy of the said Summons, Complaint and Exhibits A-B-C-D-E and F upon Fred H. Kanne, Collector of Internal Revenue, at Honolulu, T. H.

Dated at Honolulu, T. H., this 23rd day of November, A.D. 1945.

/s/ GEORGE E. BRUNS.

Subscribed and sworn to before me this 23rd day of November, A.D. 1945.

[Seal] /s/ ALFRED F. OCAMPO,  
Notary Public, First Judicial Circuit, Territory of  
Hawaii.

My Commission Expires June 30, 1949. [31]

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Territory of Hawaii  
City and County of Honolulu—ss.

I, Arthur E. Restarick, Chief Clerk of the Circuit Court of the First Judicial Circuit, Territory of Hawaii, the same being a Court of Record and having a seal, do hereby certify that Alfred F. Ocampo

before whom the foregoing acknowledgment was taken, was at the time of taking the same, A Notary Public duly sworn for the First Judicial Circuit of the Territory of Hawaii and duly authorized by the laws of said Territory to take and certify acknowledgments or proofs of deeds of land, etc., in said Territory in the manner aforesaid; that I am well acquainted with the handwriting of said Alfred F. Ocampo and verily believe that the signature to said certificate of acknowledgment is genuine. And further, that said acknowledgment was taken in accordance with the laws of the Territory of Hawaii; that I have compared the impression of the seal affixed thereto with a specimen impression thereof deposited in my office and that I believe the impression of the seal upon the original certificate is genuine.

In Testimony whereof I have hereunto set my hand and affixed the seal of said court at Honolulu aforesaid this 23rd day of November 1945.

/s/ ARTHUR E. RESTARICK,

Chief Clerk, Circuit Court First Judicial Circuit,  
Territory of Hawaii.

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[Title of District Court and Cause.]

### ANSWER

Comes now the defendant by its attorney, Ray J. O'Brien, United States Attorney for the Territory of Hawaii, and in answer to plaintiff's complaint admits and denies as follows:

1.

Admits all the allegations contained in paragraph I of plaintiff's complaint, except denies that the income taxes were illegally exacted from the plaintiff.

2.

States that he has no knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph II of the complaint.

3.

States that he has no knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph III of the complaint.

4.

Denies all the allegations contained in paragraph IV of plaintiff's complaint. [32]

5.

Denies all the allegations contained in paragraph V of plaintiff's complaint.

6.

Denies all the allegations contained in paragraph VI of plaintiff's complaint.

7.

Admits all the allegations contained in paragraph VII of plaintiff's complaint, except denies that the plaintiff inadvertently included \$3,000 of income which she purportedly assigned to her daughter-in-law and grandchildren.

8.

Denies all the allegations contained in paragraph VIII of plaintiff's complaint.

9.

Denies all the allegations contained in paragraph IX of plaintiff's complaint.

10.

Admits all the allegations contained in paragraph X of plaintiff's complaint.

11.

Admits all the allegations contained in paragraph XI of plaintiff's complaint, except denies that the tax was illegally assessed and collected from the plaintiff by the defendant.

12.

Denies all the allegations contained in paragraph XII of plaintiff's complaint.

Wherefore, defendant seeks judgment dismissing the complaint together with costs of this action.

/s/ RAY J. O'BRIEN,

United States Attorney.

[Endorsed]: Filed Feb. 27, 1946. [33]



[Title of District Court and Cause.]

MOTION TO SUBSTITUTE EXECUTRIX AS  
DEFENDANT WITH CONSENT OF EX-  
ECUTRIX.

In the above entitled cause, plaintiff shows that Fred H. Kanne, the above named defendant died on December 24, 1946, and that the Estate of said defendant has passed into the control of Agnes M. Kanne, as Executrix under the Will of said Fred H. Kanne, Deceased, said Agnes M. Kanne having qualified and been confirmed as such Executrix on February 4, 1947, as shown by the records of the Probate Court for the City and County of Honolulu, in the Territory of Hawaii.

Wherefore, plaintiff moves for an order substituting as party defendant herein, Agnes M. Kanne, Executrix as aforesaid, and that otherwise the record in the case may stand as now made and the case proceed on the pleadings and records heretofore filed in said cause. [35]

Dated: Honolulu, T. H., March 25, 1947.

ANDERSON, WRENN &  
JENKS,

By /s/ JAMES M. RICHMOND,  
Attorneys for Plaintiff.

It is agreed on behalf of the Estate of Fred H. Kanne, Deceased, that the above motion may be granted and the substitution made as therein requested.

Dated: Honolulu, T. H., March 25, 1947.

/s/ RAY J. O'BRIEN,

Attorney for Agnes M. Kanne Executrix under the  
Will and of the Estate of Fred H. Kanne, De-  
ceased.

Allowed:

Dated: March 25, 1947.

/s/ J. FRANK McLAUGHLIN,

United States District Judge.

#### Memorandum of Authorities

Sec. 58.74, Merten's Law of Federal Income Tax-  
ation, Vol. 10, pages 388, 390:

“Sec. 58.74. Suits Against Collectors. An action of assumpsit may be maintained against the collector of internal revenue who has actually collected an income tax. Such an action is personal in nature and therefore it does not abate when the collector's term expires, or upon his death. If the action against the collector has been commenced, his personal representative may be substituted as the defendant. A collector is liable to suit for taxes wrongfully collected even after his resignation or the expiration of his term. An action to recover taxes erroneously collected will not lie against the successor in office of the collector who collected the tax.”

(See also cases cited on page 390; footnotes 80 and 81.)

*Smietanka v. Indiana Steel Co.,*

257 U. S. 1, 66 L. Ed. 99, 42 S. Ct. 1.

Page 5:

“In *Patton v. Brady*, 184 U. S. 608, 46 L. Ed. 713, 22 S. Ct. Rep. 493, a suit against a collector, begun after the passage of this statute, it was held that it could be revived against his executrix, which shows again that the action is personal; as also does the fact that the collector may be held liable for interest.”

[Endorsed]: Filed March 25, 1947. [37]

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In the United States District Court for the  
Territory of Hawaii

Civil Action No. 619

LAURA D. SHERMAN,

Plaintiff,

v.

AGNES M. KANNE, Executrix under the Will of  
Fred H. Kanne, Deceased,

Defendant.

MOTION TO SUBSTITUTE EXECUTOR AS  
PLAINTIFF WITH CONSENT OF DE-  
FENDANT.

In the above entitled cause, Hawaiian Trust Com-

pany, Limited, Executor of the Will of Laura D. Sherman, deceased, shows that Laura D. Sherman, the above named plaintiff, died on June 11, 1947, and that Hawaiian Trust Company, Limited, has been qualified and confirmed as Executor of her Will on July 15, 1947, as shown by the records of the Circuit Court, First Judicial Circuit, Territory of Hawaii, in proceedings numbered Probate No. 14762.

Wherefore, Hawaiian Trust Company, Limited, Executor as aforesaid, moves for an order substituting it as such Executor as party plaintiff herein, and that otherwise the record in the case may stand as now made, and the case proceed [39] on the pleadings and records heretofore filed in said cause.

Dated: Honolulu, T. H., July 21, 1947.

/s/ JAMES M. RICHMOND,

Attorney for Hawaiian Trust Company, Limited,  
Executor of the Will of Laura D. Sherman,  
Deceased.

It is agreed by Agnes M. Kanne, Executrix under the Will and of the Estate of Fred H. Kanne, deceased, defendant, that the above Motion may be granted and the substitution be made as therein requested.

Dated: Honolulu, T. H., July 22, 1947.

/s/ RAY J. O'BRIEN,

Attorney for Agnes M. Kanne, Executrix under the  
Will and of the Estate of Fred H. Kanne,  
Deceased.



Allowed:

Dated: 7-22, 1947.

/s/ J. FRANK McLAUGHLIN,  
United States District Judge.

[Endorsed): Filed July 22, 1947. [40]

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In the United States District Court  
For the Territory of Hawaii

Civil No. 619

HAWAIIAN TRUST COMPANY, LIMITED,  
Executor of the Will of Laura D. Sherman,  
Deceased,

Plaintiff,

AGNES M. KANNE, Executrix under the Will of  
Fred H. Kanne, Deceased,

Defendant.

### STIPULATION OF FACTS

It is Hereby Stipulated by and between Hawaiian Trust Company, Limited, Executor of the Will of Laura D. Sherman, deceased, plaintiff above named, by James M. Richmond, its attorney, and Agnes M. Kanne, Executrix under the Will of Fred H. Kanne, deceased, defendant above named, by Ray J. O'Brien, United States Attorney for the District of Hawaii, her attorney, as follows:

## I.

The trust agreement, of which Exhibit A attached to plaintiff's Complaint is a copy, was duly executed and delivered, and the copy marked "Exhibit A" is a true copy thereof and may be received in evidence for all purposes for which the original might be received. [42]

## II.

Frederick Dickson Nott is a son of the said Laura D. Sherman, deceased, and was divorced from Anna Adams Nott by a decree of final divorce entered by the Circuit Court of the First Judicial Circuit, Territory of Hawaii, on April 28, 1936, in an action numbered Divorce No. 16861. The said decree directed said Frederick Dickson Nott to pay alimony in the sum of \$100 per month to the divorced wife and in addition to pay her \$75 per month each for the support and maintenance of Frederick Dickson K. Nott and Gretchen K. Nott (minor children of Frederick Dickson Nott and Anna Adams Nott, the custody of which children having been awarded to said Anna Adams Nott.

## III.

Three assignments, of which Exhibits B, C and D attached to plaintiff's Complaint are copies, were duly executed and delivered and may be received in evidence for all purposes for which the originals thereof might have been received and said copies are true copies of the originals; these assignments were made because Frederick Dickson Nott does not have sufficient income himself to pay the

amounts awarded in said decree of divorce and because the said Laura D. Sherman desired to assist him financially; on April 16, 1936, the date of said assignments, Frederick Dickson K. Nott was 10 years of age and Gretchen K. Nott was 9 years of age. [43]

Dated: Honolulu, T. H., September 19th, 1947.

HAWAIIAN TRUST

COMPANY, LIMITED,

Executor of the Will of Laura D. Sherman, Deceased, Plaintiff.

By /s/ JAMES M. RICHMOND,

Attorney for Plaintiff.

AGNES M. KANNE,

Executrix Under the Will of Fred H. Kanne, Deceased, Defendant.

By RAY J. O'BRIEN,

United States Attorney for  
the District of Hawaii,

By /s/ MAURICE SAPIENZA,

Attorney for Defendant.

Approved:

/s/ J. FRANK McLAUGHLIN,

Judge of the United States District Court for the  
District of Hawaii.

[Endorsed]: Filed Sept. 24, 1947. [44]

[Title of District Court and Cause.]

SPECIAL FINDINGS OF FACT AND  
CONCLUSIONS OF LAW

SPECIAL FINDINGS OF FACT

Upon the record and evidence adduced in this case, the Court makes the following special findings of fact:

I.

That the facts were stipulated and admitted into evidence except those facts stated in the supplementary stipulation relating to the life expectancy of Anna Adams Nott, Frederick Dickson K. Nott, Gretchen K. Nott, and Laura D. Sherman, which were not admitted in evidence, on the ground that such information was wholly immaterial in the case.

II.

That Laura D. Sherman, before her death on June 11, 1947, and during the entire taxable years 1940 and 1941 involved herein, was a citizen of the United States of America and a resident of Honolulu, Territory of Hawaii. During the entire calendar years 1940 and 1941, Laura D. Sherman was married and living with her husband. In her Federal Income Tax Return for the taxable year 1940, Mrs. Sherman claimed a personal exemption of \$2,000.00 and an earned income credit of \$300.00. In her Federal Income Tax Return for the taxable year 1941, Mrs. Sherman claimed a personal exemption of \$1,500.00 and an earned income credit of \$300.00. All of said exemptions and credits were allowed.



## III.

On December 26, 1935, George Sherman, husband of Laura D. Sherman, executed an inter vivos, irrevocable trust, in which she and the Hawaiian Trust Company, Limited, a Hawaiian corporation, were designated as trustees, and it was provided therein that all of the net income derived from the trust estate should be paid to Laura D. Sherman during her lifetime.

## IV.

That during the calendar year 1940 the trustees of the aforesaid Sherman Trust actually paid to Laura D. Sherman the total sum of \$6,332.42 of the net income of the trust estate. During the calendar year 1941, the said trustees actually paid to Laura D. Sherman the total sum of \$7,598.98 of the net income of said trust estate. [47]

## V.

Frederick Dickson Nott, son of Laura D. Sherman, was divorced from Anna Adams Nott by a decree of divorce entered on April 28, 1936, in divorce number 16,861 in the files of the Clerk of the Circuit Court, First Judicial Circuit, Territory of Hawaii. The decree ordered alimony of \$100.00 per month for the divorced wife so long as she should remain unmarried, and in addition \$75.00 per month each for the support and maintenance of Frederick Dickson K. Nott and Gretchen K. Nott, minor children of the said libellant and libellee, until the minors should have respectively attained their majorities. The custody of the children was awarded to Anna Adams Nott.

## VI.

By separate documents, each dated April 16, 1936, Laura D. Sherman made assignments of \$100.00 per month to Anna Adams Nott until death or remarriage, whichever is earlier, and \$75.00 per month for each of the minor children until the respective children's death or majority, whichever is earlier, out of the income to which Laura D. Sherman was entitled from the said trust.

The pertinent part of the assignment to Anna Adams Nott to cover monthly payments of \$100.00 for her own use read as follows:

“Now Therefore the premises considered, the undersigned, Laura D. Sherman, hereinafter referred to as the assignor, does hereby assign, transfer and set over unto Anna Adams Nott, hereinafter referred to as the assignee, the sum of One Hundred Dollars (\$100.00) a month from the income to which the assignor now is or shall be entitled to receive as life beneficiary under the terms and provisions of that certain unrecorded trust deed dated December 26, 1935, executed by George Sherman as settlor and [48] the assignor and Hawaiian Trust Company, Limited, an Hawaiian corporation. as trustees, until the death or remarriage of the assignee whichever event shall first occur and upon the occurrence of either of said events this assignment shall become inoperative and shall be of no further force or effect.

“The Hawaiian Trust Company, Limited, co-trustee under said trust deed, is hereby em-

powered and directed to pay from the assignor's income, as aforesaid, the sum of One Hundred Dollars (\$100.00) a month to the said assignee, the first of such payments to be made on the 1st day of May, 1936, and a like sum on the 1st day of each and every month thereafter until the death or remarriage of said assignee, whichever event shall first occur, and upon the occurrence of either of such events of which said Hawaiian Trust Company, Limited, shall have strict and exact proof, all payments shall cease and determine."

The pertinent part of the assignment to cover the payments of \$75.00 per month for the support and maintenance of each of the minor children reads as follows:

"Now Therefore in consideration of the premises and of the promise of the assignee hereinafter contained the assignor does hereby assign, transfer and set over unto the assignee the sum of Seventy-Five Dollars (\$75.00) a month from the income to which the assignor now is or shall be entitled to receive as life beneficiary under the terms and provisions of that certain unrecorded trust deed dated December 26, 1935, executed by George Sherman as settlor and the assignor and Hawaiian Trust Company, Limited, an Hawaiian corporation, as trustees, which sum is to be used by the assignee solely for the support, education and maintenance of said minor during his minority

provided, however, and this assignment is upon this express condition, that upon the occurrence of any of the following events this assignment shall become inoperative and all payments authorized to be made herein shall cease and determine, such events being:

- (1) Upon the death of said minor or the assignee;
- (2) Upon the said minor attaining his majority under the laws of the jurisdiction in which said minor is then living; [49]

“The Hawaiian Trust Comany, Limited, co-trustee under said trust deed, is hereby empowered and directed to pay from the assignor’s income, as aforesaid, the sum of Seventy-Five Dollars (\$75.00) a month to the said assignee, the first of such payments to be made on the 1st day of May, 1936, and a like sum on the 1st day of each and every month thereafter until the occurrence of any one or more of the above mentioned events and upon the occurrence of any of such events (of which said Hawaiian Trust Company, Limited, shall have strict and exact proof) all payments shall cease and determine.”

## VII.

The aforesaid assignments were made because Frederick Dickson Nott, son of taxpayer, did not have sufficient income himself to pay the amounts awarded in said decree of divorce and because Laura



D. Sherman desired to assist him financially. The aforesaid assignments were not made for the purpose of avoidance of taxes.

### VIII.

On April 16, 1936, the date of the assignments, Frederick Dickson K. Nott was approximately ten years of age, Gretchen K. Nott was approximately nine years of age, Anna Adams Nott was approximately thirty-five years of age, and Laura D. Sherman was approximately sixty-seven years of age.

### IX.

Pursuant to the assignments, the trustees of the aforesaid Sherman Trust paid out of the net income of that trust to Anna Adams Nott the total sum of \$1,200.00 during the calendar year 1940 and the total sum of \$1,200.00 during the calendar year 1941 for her support, and paid out of the net income of that trust to Anna Adams Nott the total sum of \$900.00 during the calendar year 1940 and the total sum of \$900.00 during the calendar year 1941, for the support and maintenance of Frederick Dickson K. Nott, minor child of [50] Anna Adams Nott; and said trustees paid out of the net income of said trust to Anna Adams Nott the total sum of \$900.00 during the calendar year 1940 and the total sum of \$900.00 during the calendar year 1941 for the support and maintenance of Gretchen K. Nott, minor child of Anna Adams Nott.

X.

Anna Adams Nott, Frederick Dickson K. Nott and Gretchen K. Nott are presently surviving and reside in the State of Washington. These persons resided in Hawaii from prior to April 16, 1936, until December 5, 1941. On the latter date, they left Hawaii and proceeded to the State of Washington, where they arrived during the year 1942 and have resided there at all times since their arrival. Under the laws of the State of Washington, the age of majority is twenty-one years. Under the laws of the Territory of Hawaii, the age of majority is twenty years.

XI.

On March 15, 1941, Laura D. Sherman filed with the Collector of Internal Revenue for the Territory of Hawaii her Federal Income Tax Return for the calendar year 1940. She included in this return \$9,332.40 representing the entire amount of the net income for the calendar year 1940 of the aforesaid Sherman Trust dated December 26, 1935, and reported in that return a taxable net income of \$26,172.86, and disclosed a tax liability of \$4,274.57, which was paid in four installments to Collector Fred H. Kanne as follows: [51]

Date Paid	Amount Paid
March 15, 1941.....	\$1,068.65
June 14, 1941.....	1,068.65
September 12, 1941.....	1,068.64
December 12, 1941.....	1,068.63
	<hr/>
	\$4,272.57

## XII.

On March 16, 1942, Laura D. Sherman filed with the same Collector of Internal Revenue her Federal Income Tax Return for the calendar year 1941. In this return, Mrs. Sherman included \$10,598.98 representing the entire amount of the net income for the calendar year 1941 of the aforesaid Sherman Trust dated December 26, 1935, and reported in that return a taxable net income of \$21,200.98, and disclosed a tax liability of \$6,046.15 which was paid in four installments to Collector Fred H. Kanne as follows:

Date Paid	Amount Paid
March 16, 1942.....	\$1,511.54
June 13, 1942.....	1,511.54
September 14, 1942.....	1,511.54
December 15, 1942.....	1,511.53
Total.....	<hr/> \$6,046.15

## XIII.

Thereafter, on August 5, 1944, Mrs. Sherman paid to Collector Fred H. Kanne a deficiency of \$90.00 in tax for the taxable year 1941, plus interest thereon of \$12.91, or a total of \$102.91, which is not involved in this controversy.

## XIV.

On March 14, 1944, Laura D. Sherman filed with the Collector of Internal Revenue at Honolulu, Hawaii, a claim for [52] refund of \$969.65, of the 1940 Federal Income Taxes paid by her and a claim for refund of \$1,434.81 of the 1941 Federal

Income Taxes paid by her. It was alleged in said claims for refund that Laura D. Sherman's distributive share of the aforesaid Sherman Trust of December 26, 1935, had been inadvertently overstated on the fiduciary return of the trustees in that trust by the sum of \$3,000.00 with respect to each of the taxable years 1940 and 1941; that Laura D. Sherman was only entitled to and actually received \$3,000.00 less than the distribution returned by the trustees as taxable to her; and Laura D. Sherman demanded an adjustment of her income for the years 1940 and 1941 by eliminating therefrom said \$3,000.00 of overstated income. Both claims were disallowed by the Commissioner of Internal Revenue, and no amount has been refunded to Laura D. Sherman on account of said total sum of \$2,404.46 claimed to be refundable with respect to the taxable years 1940 and 1941.

### XV.

That Fred H. Kanne was Collector of Internal Revenue of the United States of America for the District of Hawaii and a resident of Honolulu at all times from on or about August 1, 1933, until his death on December 24, 1946; that Agnes M. Kanne, the duly qualified and appointed Executrix of the Will and of the Estate of Fred H. Kanne, Deceased, was substituted as defendant in this cause by order of this Court on March 6, 1947.



## CONCLUSIONS OF LAW

Upon the record and evidence adduced in this case, [53] the Court makes the following conclusions of law:

## I.

The gifts of income conferred by the three respective assignments dated April 16, 1936, to Anna Adams Nott, Frederick Dickson K. Nott and Gretchen K. Nott, while substantial in amounts, were, respectively, upon the happening of any one of the conditions provided in said assignments, brought to an end and the respective assignment thereupon terminated.

## II.

Laura D. Sherman, the assignor, retained the entire reversionary interest in the income so assigned, which reversion, representing as it does a substantial economic interest in the Sherman Trust dated December 26, 1935, definitely requires the inclusion of the assigned income as part of the taxable gross income of the assignor under the provisions of Sec. 22(a) of the Internal Revenue Code and the applicable Treasury Regulations promulgated thereunder, and brings the taxability of such assigned income within the rationale of the Supreme Court's opinion in the case of *Harrison v. Schaffner*, 312 U. S. 579, and excludes it from the rationale of the Supreme Court's opinion in the case of *Blair v. Commissioner*, 300 U. S. 5, relied upon by the plaintiff herein.

III.

The defendant is sustained in his objection to the admissibility in evidence of the data set out in paragraphs VIII, IX, X and XI of the Supplementary Stipulation of Facts, respecting the life expectancies of the individuals named in said paragraph, on the ground that such information is [54] immaterial for any purposes in this case.

IV.

I conclude that judgment should be entered for the defendant, and the complaint herein dismissed, together with costs assessed against the plaintiff, and that a judgment order be entered accordingly.

Entry of judgment is hereby directed to be entered in conformity with the foregoing special findings of fact and conclusions of law.

Dated: November 20, 1947.

/s/ DELBERT E. METZGER.

[Endorsed]: Filed Nov. 21, 1947. [55]

In the District Court of the United States  
for the District of Hawaii

Civil No. 619

HAWAIIAN TRUST CO., LIMITED, Executor  
of the Will of Laura D. Sherman, Deceased,  
Plaintiff,

vs.

AGNES M. KANNE, Executrix under the Will of  
Fred H. Kanne, Deceased,  
Defendant.

### JUDGMENT OF DISMISSAL

Be it remembered that on November 10, 1947, there came on for trial the above-entitled and numbered action wherein this case having been submitted upon the pleadings, and stipulation of facts, and evidence having been adduced, and the Court being sufficiently advised, and having made and filed its opinion and findings of fact and conclusions of law herein, now therefore and in pursuance thereto,

It is hereby ordered and adjudged that the plaintiff have and recover nothing from Agnes M. Kanne, Executrix under the will of Fred H. Kanne, deceased, the defendant, and defendant have judgment herein dismissing the complaint with lawful costs in the action, for which let execution issue.

Signed at Honolulu, T. H., this 16th day of February, 1948.

/s/ DELBERT E. METZGER,  
United States District Judge.  
JAMES M. RICHMOND,  
Attorney for Plaintiff.  
RAY J. O'BRIEN,

United States Attorney for the District of Hawaii,  
Attorney for Defendant.

Approved as to form only, and expressly not approved as to contents.

/s/ JAMES M. RICHMOND,  
Attorney for Plaintiff.

Receipt of a copy of the within Judgment of Dismissal is hereby acknowledged this 11th day of February, 1948.

/s/ JAMES M. RICHMOND.

Entry of Judgment of Dismissal in Civil Docket on February 18, 1948.

/s/ E. C. ROBINSON,  
Deputy Clerk.

[Endorsed]: Filed February 17, 1948. [56]

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From the Minutes of the United States District  
Court for the District of Hawaii

Monday, November 10, 1947

[Title of Cause.]

On this day came Mr. James M. Richmond of the firm Anderson, Wrenn, & Jenks, counsel for the



plaintiff herein, and also came Mr. Leland T. Atherton, Special Assistant to the Attorney General of the United States, and Mr. Edward A. Towse, Assistant United States District Attorney, counsel for the defendant herein. This case was called for trial.

Certified copy of Decree of Divorce, Anna Adams Nott and F. Dickson Nott, was admitted in evidence as Plaintiff's Exhibit "A," marked and ordered filed.

Certificate of Assessments and Payments was admitted in evidence as Defendant's Exhibit No. 1 marked and ordered filed.

At 10:30 a.m., both sides rested.

Argument was then had by Mr. Richmond, followed at 11:15 a.m., by argument by Mr. Atherton.

At 11:35 a.m., the Court ordered that this case be continued at 1:45 p.m. this day.

At 1:48 p.m., Mr. Atherton continued his argument.

At 2:15 p.m., following the conclusion of argument, the Court stated that from the facts of the case and cases cited the Court was compelled to hold in favor of the defendant. The complaint was ordered dismissed and counsel for the government was ordered to prepare the findings of fact and conclusions of law. [57a]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice is hereby given that Hawaiian Trust Company, Limited, Executor of the Will of Laura D. Sherman, deceased, plaintiff above named, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit from the final judgment of dismissal entered in this action on February 17, 1948.

/s/ JAMES M. RICHMOND,  
Attorney for Appellant, Hawaiian Trust Company,  
Limited, Executor of the Will of Laura D.  
Sherman, Deceased.

[Endorsed]: Filed March 17, 1948. [59]

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[Title of District Court and Cause.]

BOND FOR COSTS ON APPEAL

Know All Men by These Presents, that we, Hawaiian Trust Company, Limited, Executor of the Will of Laura D. Sherman, deceased, as principal, and Home Insurance Company of Hawaii, as surety, are held and firmly bound unto Agnes M. Kanne, Executrix under the Will of Fred H. Kanne, deceased, in the full and just sum of Two Hundred Fifty Dollars (\$250.00) to be paid to the said Agnes M. Kanne, Executrix under the Will of Fred H. Kanne, deceased, her successors and assigns, to

which payment, well and truly to be made, we bind ourselves, our successors and assigns, jointly and severally, by these presents, sealed with our seals and dated this 16th day of March, 1948.

Whereas on February 17, 1948, in an action pending in the District Court of the United States for the District of Hawaii, between Hawaiian Trust Company, Limited, Executor of the Will of Laura D. Sherman, deceased, as plaintiff, and Agnes M. Kanne, Executrix under the Will of Fred H. Kanne, deceased, as [61] defendant, a judgment of dismissal was rendered against the said Hawaiian Trust Company, Limited, Executor of the Will of Laura D. Sherman, Deceased, and the said Hawaiian Trust Company Limited, Executor of the Will of Laura D. Sherman, deceased, having filed a notice of appeal from such judgment of dismissal to the United States Circuit Court of Appeals for the Ninth Circuit;

Now the condition of this obligation is such that if the said Hawaiian Trust Company, Limited, Executor of the Will of Laura D. Sherman, deceased, shall prosecute its appeal to effect and shall pay costs if the appeal be dismissed or the judgment affirmed, or such costs as the said Ninth Circuit Court of Appeals may award against the said Hawaiian Trust Company, Limited, Executor of the Will of Laura D. Sherman, deceased, if the judgment is modified, or in any other event, then

this obligation to be void; otherwise to remain in full force and effect.

HAWAIIAN TRUST  
COMPANY, LIMITED,  
Executor of the Will of  
Laura D. Sherman,  
Deceased.

By /s/ CARTER GALT,  
Its Vice President.

By /s/ L. A. WILLS,  
Its Asst. Vice Pres.

[Seal] HOME INSURANCE  
COMPANY OF HAWAII,

By /s/ A. L. WOODDELL,  
Attorney in Fact.

By /s/ MARY HINDS,  
Attorney in Fact. [32]

Territory of Hawaii,  
City and County of Honolulu—ss.

On this 16th day of March, 1948, before me appeared A. L. Wooddell, and Mary Hinds, to me personally known, who, being by me severally duly sworn, did say that they are respectively the Attorneys-in-fact of the Home Insurance Company of Hawaii, Limited, a corporation of the Territory of Hawaii, duly appointed under Power of Attorney dated the 2nd day of February, 1948, which power of attorney is now in full force and effect; and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed on behalf of said corporation



under the authority of its Board of Directors, and said A. L. Wooddell and Mary Hinds, severally acknowledge said instrument to be the free act and deed of said corporation.

[Seal]        /s/ ARCHIE IWANAGA,  
Notary Public, First Judicial Circuit, Territory of  
Hawaii.

My Commission expires June 30, 1949.

Territory of Hawaii,  
City and County of Honolulu—ss.

On this 16th day of March, 1948, before me personally appeared Carter Galt and L. A. Wills, to me known, who being by me duly sworn did say that they are Vice President and Asst. Vice President, respectively, of Hawaiian Trust Company, Limited; that the seal affixed to the foregoing instrument is the corporate seal of said corporation; that said instrument was signed and sealed in behalf of said corporation by authority of its Board of Directors; and the said Carter Galt and L. A. Wills acknowledged said instrument to be the free act and deed of said corporation.

[Seal]        /s/ ETHEL BALCOM,  
Notary Public, First Judicial Circuit, Territory of  
Hawaii.

My Commission expires August 29, 1951.

[Endorsed]: Filed March 17, 1948. [63]

[Title of District Court and Cause.]

DESIGNATION OF RECORD ON APPEAL

To the Clerk of the United States District Court  
for the District of Hawaii:

Please prepare and certify a transcript of the record in this case, to be filed with the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, upon the appeal herein, and include in such transcript the following:

1. Complaint, Exhibits A, B, C, D, E, and F, and Summons.
2. Answer.
3. Motion to Substitute Executrix as Defendant with Consent of Executrix.
4. Motion to Substitute Executor as Plaintiff with Consent of Defendant.
5. Stipulation of Facts.
6. Supplementary Stipulation. [65]
7. Plaintiff's Exhibit "A."
8. Defendant's Exhibit #1.
9. Special Findings of Fact and Conclusions of Law.
10. Judgment of Dismissal.
11. This Designation of Record on Appeal.
12. Statement of Points Relied Upon on Appeal.
13. Order Extending Time to File and Docket Records with the United States Circuit Court of Appeals for the Ninth Circuit.

Dated: Honolulu, T. H., March 25, 1948.

/s/ JAMES M. RICHMOND,  
Attorney for Appellant.

[Endorsed]: Filed March 28, 1948. [66]

[Title of District Court and Cause.]

STATEMENT OF POINTS RELIED  
UPON ON APPEAL

Comes now Hawaiian Trust Company, Limited, appellant herein, and states that the points upon which it intends to rely on appeal in this case are as follows:

1. The Court erred in making and entering its Special Findings of Fact and Conclusions of Law dated November 20, 1947, in the above cause.

2. The Court erred in rendering and entering Judgment of Dismissal dated February 17, 1948, in the above cause.

3. The evidence respecting the life expectancies of Laura D. Sherman, Anna Adams Nott, Frederick Dickson K. Nott and Gretchen K. Nott was relevant to show that the possibility of a reverter to Laura D. Sherman of the assigned interest was remote, and the Court erred in excluding as immaterial such evidence offered by the appellant.

4. Each of the three assignments dated April 16, 1936, constituted a transfer of a portion of the equitable [68] interest of Laura D. Sherman in the corpus of the trust dated December 26, 1935, and the Court erred in not so finding and deciding.

5. Income paid to the assignees by virtue of said assignments was not taxable to Laura D. Sherman, and plaintiff is entitled to recover income taxes paid by Laura D. Sherman on account of said income, and the Court erred in not giving judgment for plaintiff accordingly.

6. Each of the three assignments dated April 16, 1936, was a substantial disposition of the particular interest of Laura D. Sherman in the trust dated December 26, 1935 thus assigned, and the Court erred in finding and deciding that the income from such assigned interests was taxable to the assignor, Laura D. Sherman.

7. The reversionary interest of Laura D. Sherman in the interests transferred by the said three assignments was not substantial, particularly in relation to the interests transferred, and the Court erred in finding and deciding that the said reversionary interest was a substantial economic interest in the trust dated December 26, 1935.

8. The Court erred in finding and deciding that the retention of the reversionary interest by Laura D. Sherman in the interests assigned by her as aforesaid required the inclusion in her taxable gross income of income paid to the assignees by virtue of the said assignments.

9. The Court erred in finding and deciding that the facts of this case are controlled by the decision in *Harrison [69] v. Schaffner*, 312 U. S. 79 rather than *Blair v. Commissioner*, 300 U. S. 5.

Dated at Honolulu, Hawaii, March 24, 1948.

HAWAIIAN TRUST

COMPANY, LIMITED,

Executor of the Will of Laura  
D. Sherman, Deceased.

By /s/ JAMES M. RICHMOND,

Attorney for Appellant.

[Endorsed]: Filed March 29, 1948. [70]



[Title of District Court and Cause.]

CERTIFICATE OF CLERK, U. S. DISTRICT  
COURT, TO TRANSCRIPT OF RECORD  
ON APPEAL

United States of America,  
District of Hawaii—ss.

I, Wm. F. Thompson, Jr., Clerk of the United States District Court for the District of Hawaii, do hereby certify that the foregoing pages numbered 1 to 72, inclusive, are a true and complete transcript of the record and proceedings had in said court in the above-entitled cause, as the same remains of record and on file in my office, and that the costs of the foregoing transcript of record are \$9.70 and that said amount has been paid to me by the appellant.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court, this 19th day of April 1948.

[Seal]      /s/ WM. F. THOMPSON, JR.,  
Clerk, United States District  
Court, District of Hawaii.

PLAINTIFF'S EXHIBIT A

In the Circuit Court of the First Judicial Circuit  
Territory of Hawaii, Division of Domestic  
Relations

D. No. 16861

At Chambers—In Divorce

ANNA ADAMS NOTT,

Libellant,

vs.

F. DICKSON NOTT,

Libellee.

1st Circuit Court, Territory of Hawaii. Filed  
1936 Apr. 28 AM 9 10. Chas K. Buchanan (s),  
Clerk.

DECREE OF DIVORCE

On this 28th day of April, A. D. 1936, at the  
courthouse in the City and County of Honolulu,  
Territory of Hawaii, in the public court room of  
the judge of said court, came on to be heard the  
libel of the above named libellant, praying that the  
bonds of matrimony heretofore and then existing  
between the said Anna Adams Nott and F. Dickson  
Nott be dissolved by reason of the desertion by the  
libellee of the libellant, Frank E. Thompson, Esq.,  
appearing for the libellant, and William B. Lymer,  
Esq., appearing for the libellee, and the said libel-  
lant being present in court, strict and exact proof  
was made to this court by the libellant that the  
said parties are legally intermarried, and that the

allegations in her libel are true, and the court having heard all the evidence and being fully advised in the premises, does find:

That the allegations in the libel are true.

It Is Therefore Ordered, Adjudged and Decreed that the bonds of matrimony heretofore and now existing between the said Anna Adams Nott and F. Dickson Nott be and the same are hereby dissolved by reason of the desertion by the libellee of the libellant.

It Is Further Ordered, Adjudged and Decreed that the care, custody and control of Frederick Nott, a boy, and Gretchen Nott, a girl, minor children of said marriage, be and it is hereby awarded to said libellant, with the right of the libellee to visit said minor children at any and all reasonable times.

It Is Further Ordered, Adjudged and Decreed that said minor children may be removed from the jurisdiction of this court, to wit, to the State of Washington, or elsewhere on the mainland of the United States; that until the further order of the court herein, the said libellee shall pay for the care, custody, education and maintenance of said children, the sum of Seventy-Five Dollars (\$75.00) monthly to each minor child and until said minor children shall have respectively achieved their majority.

And it appearing to the court by the admission of counsel that all property rights have been adjusted between the parties and with the consent of the parties hereto, which consent is

evidenced by the signatures of the libellant and libellee in the margin hereof,

/s/ ANNA ADAMS NOTT,

Libellant.

/s/ F. DICKSON NOTT,

Libellee.

It Is Further Ordered, Adjudged and Decreed that said libellee shall pay to said libellant as alimony during the time she shall remain unmarried, the sum of One Hundred Dollars (\$100.00) per month.

All payments hereunder shall be made through the clerk of the above entitled court, the first payment upon the signing of this decree.

This Decree Shall Take Effect From and After the Date Hereof.

[Seal] /s/ F. M. BROOKS,

Judge of the above entitled  
court.

OK

/s/ F. E. THOMPSON.

OK

/s/ WILLIAM B. LYMER.

I do hereby certify that the foregoing is a full, true and correct copy of the original on file in this office.

[Seal] /s/ MAYDEEN I. FULLER,

Clerk, Circuit Court, First  
Circuit, Territory of  
Hawaii.



## PLAINTIFF'S EXHIBIT "B"

In the United States District Court  
for the Territory of Hawaii

Civil No. 619

HAWAIIAN TRUST COMPANY, LIMITED,  
Executor of the Will of Laura D. Sherman,  
Deceased,

Plaintiff,

vs.

AGNES M. KANNE, Executrix under the Will  
of Fred H. Kanne, Deceased,

Defendant.

Admitted in Evidence subject to objection as to  
relevancy of certain sections. /s/ D. E. Metz-  
ger, Judge.

## SUPPLEMENTARY STIPULATION

It Is Hereby Stipulated by and between the parties hereto through their respective attorneys that the following statements of fact shall be considered as true. It is also agreed by and between the parties hereto that they may also produce oral testimony at the trial of this case and offer any additional evidence, documentary or otherwise, provided such additional evidence shall not vary or in any way contradict or conflict with the facts herein stipulated to be taken as true, and provided further that such additional evidence is properly admissible.

## I.

On December 26, 1935, George Sherman, husband of Laura D. Sherman, entered into an agreement with Laura D. Sherman and Hawaiian Trust Company, Limited, a Hawaiian corporation, said agreement being that hereinbefore described in the complaint as Exhibit "A" and incorporated herein by reference and made a part hereof for all purposes. Said agreement created an irrevocable trust by which Laura D. Sherman and Hawaiian Trust Company, Limited, were trustees and provided that all of the net income derived from the trust estate thereby created be paid to Laura D. Sherman during her lifetime.

## II.

During the calendar year 1940 the said trustees actually paid to Laura D. Sherman the total amount of \$6,332.40 of the net income of said trust estate. During the calendar year 1941 the said trustees actually paid to Laura D. Sherman the total sum of \$7,598.98 of the net income of said trust estate.

## III.

On March 15, 1941, Mrs. Laura D. Sherman filed with the Collector of Internal Revenue for the District of Hawaii her federal income tax return for the calendar year 1940. Mrs. Sherman included in this return \$9,332.40 representing the entire amount of the net income for the calendar year 1940 of the trust dated December 26, 1935, hereinbefore described as Exhibit A and reported in that return a taxable net income of \$26,172.86, and dis-

said Anna Adams Nott pursuant to said assignments. Pursuant to the assignment described as Exhibit "B," said trustees paid out of the net income of said trust to said Anna Adams Nott the total sum of \$1200 during the calendar year 1940, and the total sum of \$1200 during the calendar year 1941. Pursuant to the assignment described as Exhibit "C," said trustees paid out of the net income of said trust to said Anna Adams Nott the total sum of \$900 during the calendar year 1940, and the total sum of \$900 during the calendar year 1941. Pursuant to the assignment described as Exhibit "D," said trustees paid out of the net income of said trust to said Anna Adams Nott the total sum of \$900 during the calendar year 1940, and the total sum of \$900 during the calendar year 1941.

### VIII.

Said Anna Adams Nott, divorced wife of Frederick Dickson Nott, was born in Honolulu, Hawaii, on April 28, 1901. On or about April 16, 1936 her age was approximately 34 years, 11 months. The Combined or Actuaries Experience Tables (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 30.93 years. The American Experience Table of Mortality (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 31.84 years. The defendant objects to the admissibility in evidence of information showing the life expectancy of Anna Adams Nott as of on or about April 16, 1936, on

the ground that such information is immaterial and irrelevant to the issue involved in this proceeding.

### IX.

Said Frederick Dickson K. Nott, son of said Anna Adams Nott, was born in Honolulu, Hawaii, on November 22, 1925. On or about April 16, 1936, his age was approximately ten years, five months. The Combined or Actuaries Experience Tables (printed in Wolfe, *Inheritance Tax Calculations* (2nd Ed.)) states that the life expectancy of a person of that age is 48.08 years. The American Experience Table of Mortality (printed in Wolfe, *Inheritance Tax Calculations* (2nd Ed.)) states that the life expectancy of a person of that age is 48.46 years. The defendant objects to the admissibility in evidence of information showing the life expectancy of Frederick Dickson K. Nott as of on or about April 16, 1936, on the ground that such information is immaterial and irrelevant to the issue involved in this proceeding.

### X.

Said Gretchen K. Nott, daughter of said Anna Adams Nott, was born in Honolulu, Hawaii, on December 27, 1926. On or about April 16, 1936, her age was approximately nine years, four months. The Combined or Actuaries Experience Tables (printed in Wolfe, *Inheritance Tax Calculations* (2nd Ed.)) states that the life expectancy of a person of that age is 48.80 years. The American Experience Table of Mortality (printed in Wolfe, *Inheritance Tax Calculations* (2nd Ed.)) states



that the life expectancy of a person of that age is 49.14 years. The defendant objects to the admissibility in evidence of information showing the life expectancy of Gretchen K. Nott as of on or about April 16, 1936, on the ground that such information is immaterial and irrelevant to the issue involved in this proceeding.

## XI.

Said Laura D. Sherman, mother of said Frederick Dickson Nott, was born on July 27, 1869. On or about April 16, 1936, her age was approximately 66 years, 9 months. The Combined or Actuaries Experience Tables (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 10.085 years. The American Experience Table of Mortality (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 10.13 years. The defendant objects to the admissibility in evidence of information showing the life expectancy of Laura D. Sherman as of on or about April 16, 1936, on the ground that such information is immaterial and irrelevant to the issue involved in this proceeding.

## XII.

Said Anna Adams Nott, Frederick Dickson K. Nott and Gretchen Nott are presently surviving and reside in the State of Washington. Said persons resided in Hawaii from prior to April 16, 1936, until December 5, 1941. On December 5, 1941, said persons left Hawaii, proceeding to the State of Wash-

ington. Said persons arrived in Washington during the year 1942 and have resided there at all times since arrival. Under the laws of the State of Washington the age of majority is twenty-one years. (Remingtons Revised Statutes, Sections 10548, 10549.) Under the laws of the Territory of Hawaii the age of majority is twenty years. (Revised Laws of Hawaii, 1945, Section 12261.) Laura D. Sherman died June 11, 1947.

Dated at Honolulu, Hawaii, November 7, 1947.

HAWAIIAN TRUST

COMPANY, LIMITED,

Executor of the Will of Laura D. Sherman, Deceased, Plaintiff,

By /s/ JAMES M. RICHMOND,

Its Attorney.

AGNES M. KANNE,

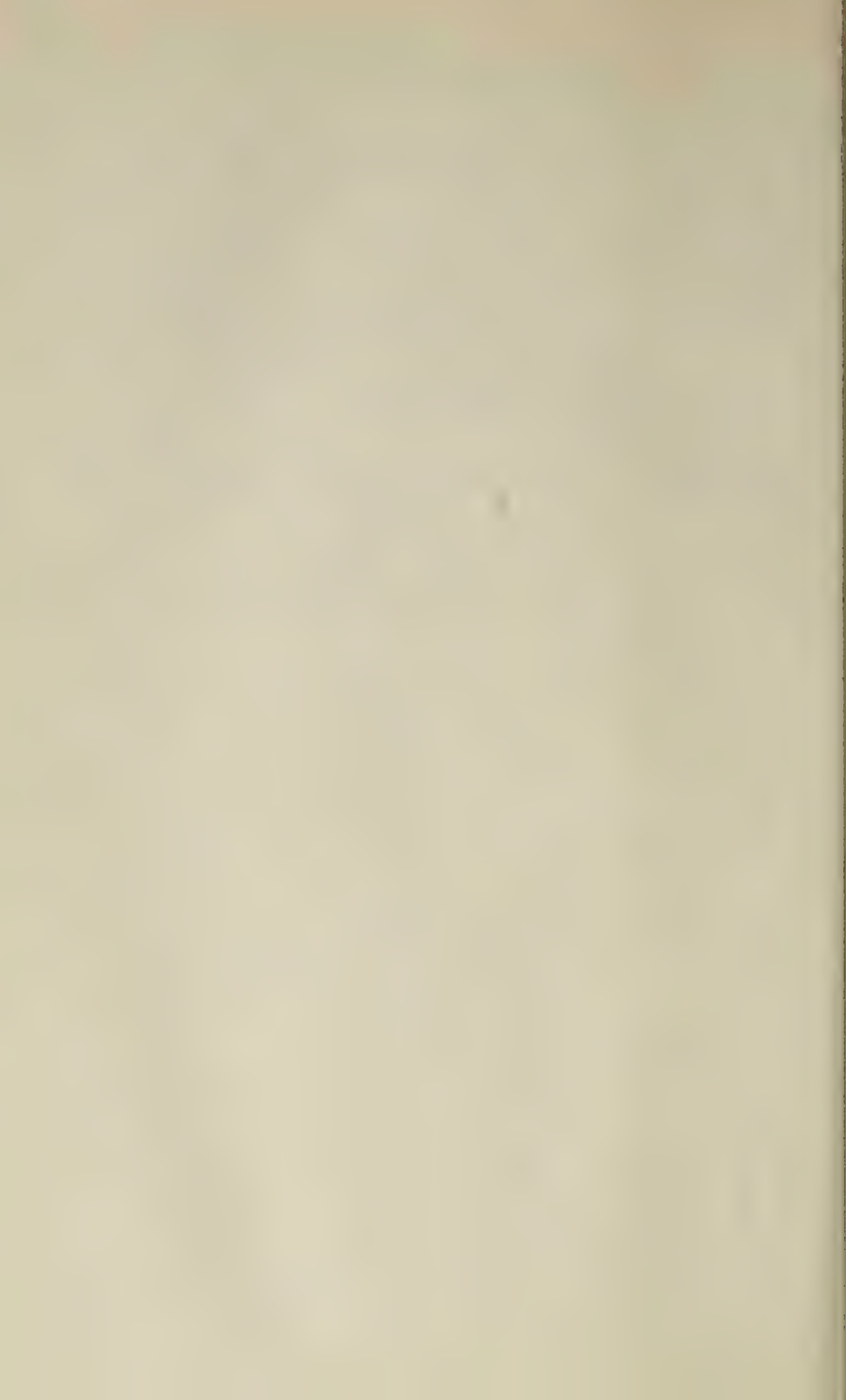
Executor under the Will of Fred H. Kanne, Deceased, Defendant.

By /s/ RAY J. O'BRIEN,

United States Attorney for  
the District of Hawaii.

By /s/ RAY J. O'BRIEN,

Attorney for Defendant.



DEPT'S EXHIBIT

# CERTIFICATE OF ASSESSMENTS AND PAYMENTS

11909

#1

OFFICE OF COLLECTOR OF INTERNAL REVENUE

In re: Laura S. Sherman

(Name of taxpayer)

DISTRICT OF HAWAII

c/o Har's Trust Co., Honolulu, T.H.

(Address)

To ~~THE COMMISSIONER OF INTERNAL REVENUE~~

ATTENTION:

Mr. Leland T. Atherton

Special Assistant to the Attorney General

(Refer to symbols and date of letter requesting this certification)

The following is a transcript of the records of this office covering the accounts of the taxpayer named

**Income Tax**

above in respect to

(Character of tax)

for the taxable years 1940 and 1941

(Period covered)

1. TAX- ABLE PERIOD	2. LIST AND YEAR	3. ACCT. NO. OR PAGE AND LINE	4. AMOUNT ASSESSED		PAID, ABATED, OR CREDITED		7. PAID AS. CE.	8. ADJUSTMENT OF OVERASSESSMENTS	
					5. DATE OR SCHEDULE NO.	6. AMOUNT			
1940	Mar/41	30612	4774	97	3-15-41	1046	65	PE	Refund filed
					6-14-41	1046	65	PE	3-9-43 Amt. 171.44
					9-12-41	1046	64	PE	allowed IT-90648
					12-12-41	1046	63	PE	2-10-44
									Refund filed
									3-14-44 Amt. 969.65
									Rejected Sch. 30032
									3-3-45
1941	May/42	306703	6046	15	3-16-42	1511	54	PE	Refund filed
					6-13-42	1511	54	PE	3-14-44
					9-14-42	1511	54	PE	Amt. 1,434.81
					12-15-42	1511	53	PE	Rejected Sch. 30032
									5-3-45
1941	Aug-25-1944	518103/1944	90	80					
BAR			Int 12	91	8-8-44	102	91	PE	
			(Int to 8-5-44)						

I CERTIFY that the foregoing transcript of the accounts of the taxpayer named above in respect to the taxes specified, is true and complete for the period stated, and that all assessments and payments of tax, penalty and interest, and all abatements, credits, and refunds relating thereto as disclosed by the records of this office, are shown therein.

Date of certificate October 27 19 47

85





[Endorsed]: No. 11909. United States Circuit Court of Appeals for the Ninth Circuit. Hawaiian Trust Company, Limited, Executor of the Will of Laura D. Sherman, Appellant, vs. Agnes M. Kanne, Executrix under the Will of Fred H. Kanne, Deceased, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Territory of Hawaii.

Filed April 23, 1948.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals  
for the Ninth Circuit.

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The United States Circuit Court of Appeals  
for the Ninth Circuit

No. 11909

HAWAIIAN TRUST COMPANY, LIMITED,  
Executor of the Will of Laura D. Sherman,  
Appellant,

vs.

AGNES M. KANNE, Executrix under the Will of  
Fred H. Kanne, Deceased,  
Appellee.

STATEMENT OF POINTS TO BE RELIED  
UPON AND DESIGNATION OF THE  
RECORD TO BE PRINTED

Comes now Hawaiian Trust Company, Limited,  
Executor of the Will of Laura D. Sherman, the

Appellant in the above entitled cause, and states that the points upon which it intends to rely in this court in this case are as follows:

I.

The District Court of the United States for the District of Hawaii erred in making and entering its Special Findings of Fact and Conclusions of Law dated November 20, 1947, in the above cause.

II.

The District Court of the United States for the District of Hawaii erred in rendering and entering Judgment of Dismissal dated February 17, 1948, in the above cause.

III.

The evidence respecting the life expectancies of Laura D. Sherman, Anna Adams Nott, Frederick Dickson K. Nott and Gretchen K. Nott was relevant to show that the possibility of a reverter to Laura D. Sherman of the assigned interest was remote, and the District Court of the United States for the District of Hawaii erred in excluding as immaterial such evidence offered by the appellant.

IV.

Each of the three assignments dated April 16, 1936, constituted a transfer of a portion of the equitable interest of Laura D. Sherman in the corpus of the trust dated December 26, 1935, and the District Court of the United States for the District of Hawaii erred in not so finding and deciding.

Income paid to the assignees by virtue of said assignments was not taxable to Laura D. Sherman, and appellant is entitled to recover income taxes paid by Laura D. Sherman on account of said income, and the District Court of the United States for the District of Hawaii erred in not giving judgment for appellant accordingly.

#### VI.

Each of the three assignments dated April 16, 1936, was a substantial disposition of the particular interest of Laura D. Sherman in the trust dated December 26, 1935, thus assigned, and the District Court of the United States for the District of Hawaii erred in finding and deciding that the income from such assigned interests was taxable to the assignor, of Laura D. Sherman.

#### VII.

The reversionary interest of Laura D. Sherman in the interests transferred by the said three assignments was not substantial, particularly in relation to the interests transferred, and the District Court of the United States for the District of Hawaii erred in finding and deciding that the said reversionary interest was a substantial economic interest in the trust dated December 26, 1935.

#### VIII.

The District Court of the United States for the District of Hawaii erred in finding and deciding that the retention of the reversionary interest by



Laura D. Sherman in the interests assigned by her as aforesaid required the inclusion in her taxable gross income of income paid to the assignees by virtue of the said assignments.

IX.

The District Court of the United States for the District of Hawaii erred in finding and deciding that the facts of this case are controlled by the decision in *Harrison v. Schaffner*, 312 U. S. 79 rather than *Blair v. Commissioner*, 300 U. S. 5.

Appellant further states that all of the transcript of record filed in this court is deemed necessary to be printed for the consideration of the points set forth above.

Dated at Honolulu, Hawaii, April 21, 1948.

HAWAIIAN TRUST

COMPANY, LIMITED,

Executor of the Will of Laura D. Sherman, Deceased.

By /s/ JAMES M. RICHMOND,

Attorney for Appellant.

[Endorsed]: Filed April 23, 1948.

United States  
CIRCUIT COURT OF APPEALS  
*For the Ninth Circuit*

HAWAIIAN TRUST COMPANY, LIMITED,  
Executor of the Will of Laura D. Sherman,  
Deceased,  
Appellant,

vs.

AGNES M. KANNE,  
Executrix under the Will of Fred H. Kanne,  
Deceased,  
Appellee.

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OPENING BRIEF FOR HAWAIIAN TRUST COMPANY, LIMITED, EXECUTOR OF THE WILL OF LAURA D. SHERMAN, DECEASED, APPELLANT

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*Upon Appeal from the District Court of the United States for the Territory of Hawaii*

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JAMES M. RICHMOND,  
Attorney for Petitioner.

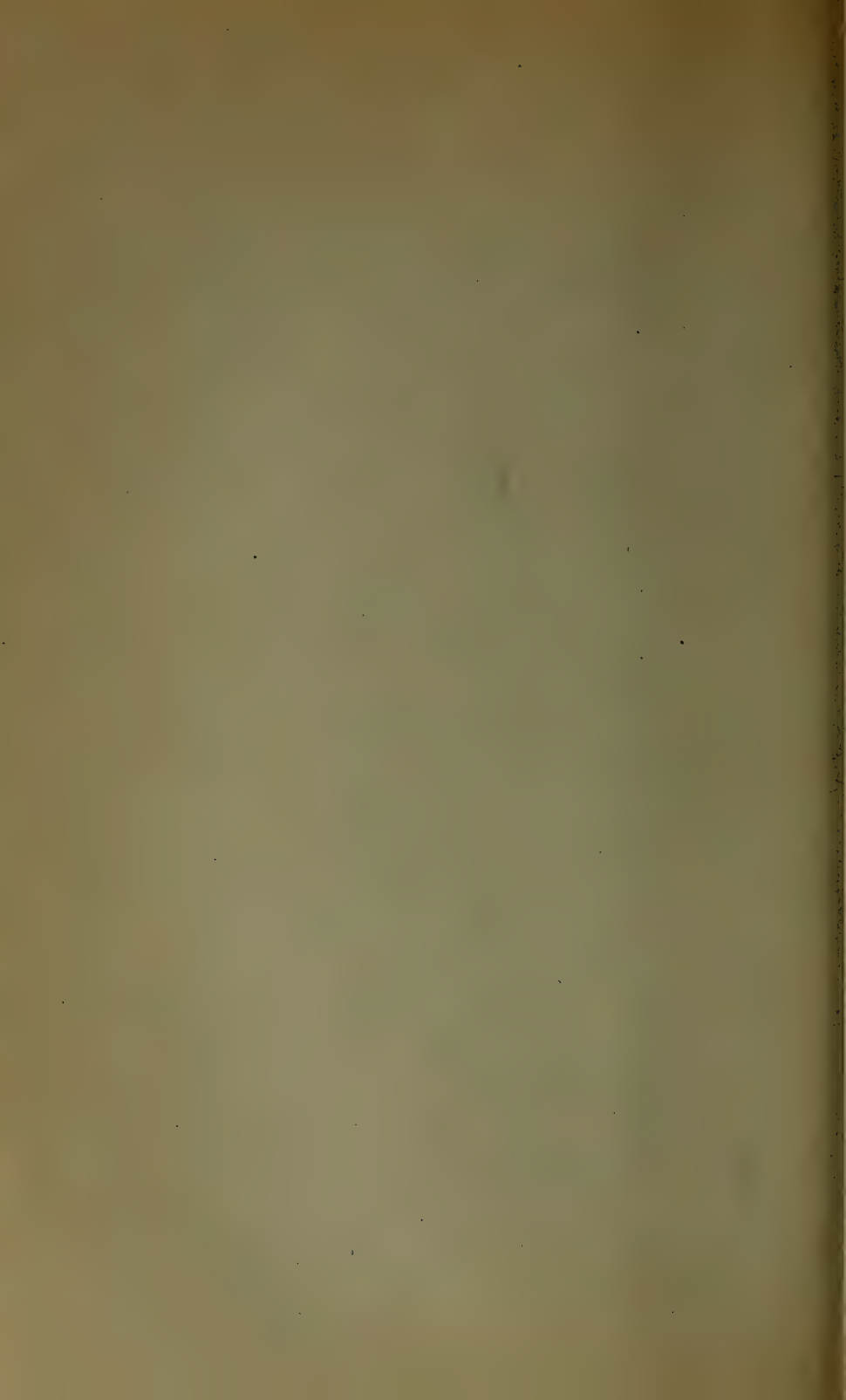
ANDERSON, WRENN & JENKS,  
Honolulu, Hawaii,  
Of Counsel.

FILE

AUG 9 - 1943

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PAUL P. O'BRIEN,



## SUBJECT INDEX

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	Pages
STATEMENT SHOWING JURISDICTION.....	1
STATEMENT OF THE CASE .....	3
SPECIFICATION OF ERRORS:	
Specification of Error No. 1 .....	5
Specification of Error No. 2 .....	6
Specification of Error No. 3 .....	6
Specification of Error No. 4 .....	8
Specification of Error No. 5 .....	9
Specification of Error No. 6 .....	9
Specification of Error No. 7 .....	9
Specification of Error No. 8 .....	10
Specification of Error No. 9 .....	10
SUMMARY OF ARGUMENT .....	10
ARGUMENT .....	11

## TABLE OF CASES

---

	Pages
<i>Belknap v. Glenn</i> , 55 Supp. 631 .....	15, 17
<i>Blair v. Commissioner</i> , 300 U.S. 5, 57 S. Ct. 330 .....	10, 12, 13, 14, 16, 17, 21
<i>Burnet v. Leininger</i> , 285 U.S. 136, 52 S. Ct. 345....	11
<i>Commissioner v. Jonas</i> , 122 Fed. (2d) 169.....	17, 18
<i>Farkas v. Commissioner</i> , 8 T.C. 1351 .....	17
<i>Harrison v. Schaffner</i> , 312 U.S., 579, 61 S. Ct. 759 .....	10, 13, 14, 15, 16, 17, 20
<i>Helvering v. Clifford</i> , 309 U.S. 331, 60 S. Ct. 554 .....	13, 14, 17, 20
<i>Helvering v. Eubank</i> , 311 U.S. 122, 61 S. Ct. 149....	11
<i>Helvering v. Horst</i> , 311 U.S. 112, 61 S. Ct. 144.....	11
<i>Huber v. Helvering</i> , 117 F. (2d) 782 .....	15
<i>Hyman v. Nunan</i> , 143 F. (2d) 425 .....	15
<i>Lucas v. Earl</i> , 281 U.S. 111, 50 S. Ct. 241 .....	11
<i>Mahaffey v. Helvering</i> , 140 F. (2d) 879.....	15, 17



## TABLE OF STATUTES

---

	Pages
INTERNAL REVENUE CODE, Sec. 22(a) . . .	5, 11
INTERNAL REVENUE CODE, Sec. 161(a) . . .	5, 11
INTERNAL REVENUE CODE, Sec. 162(b) . . .	5, 11
UNITED STATES CODE, Title 28, Sec. 41(5); (Act of March 2, 1929, Chapter 488, Sec. 1, 45 Stat. 1475) . . . . .	2
UNITED STATES CODE, Title 28, Sec. 225; (Judiciary Code, Sec. 128) . . . . .	2



**United States**  
**CIRCUIT COURT OF APPEALS**  
*For the Ninth Circuit*

HAWAIIAN TRUST COMPANY, LIMITED,  
Executor of the Will of Laura D. Sherman,  
Deceased,  
Appellant,

vs.

AGNES M. KANNE,  
Executrix under the Will of Fred H. Kanne,  
Deceased,  
Appellee.

---

OPENING BRIEF FOR HAWAIIAN TRUST COMPANY, LIMITED, EXECUTOR OF THE WILL OF LAURA D. SHERMAN, DECEASED, APPELLANT

---

*Upon Appeal from the District Court of the United States for the Territory of Hawaii*

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**STATEMENT SHOWING JURISDICTION**

This is a civil action commenced in the United States District Court for the Territory of Hawaii by

a citizen of the Territory of Hawaii by Complaint (Tr. p. 4-29) against Fred H. Kanne, Collector of Internal Revenue of the United States for the District of Hawaii for the recovery of income taxes paid, it being alleged in said Complaint that said taxes were illegally assessed and collected by defendant.

The defendant duly filed an answer (Tr. p. 31-33) to the Complaint. Thereafter defendant died and his executrix was substituted as defendant by order of the said Court on motion by plaintiff (Tr. p. 34-36). Then plaintiff died and her executor was substituted as plaintiff by order of the said Court on motion of the executor (Tr. p. 36-38). The United States District Court for the Territory of Hawaii had jurisdiction of the action under the Act of March 2, 1929, Chapter 488, Section 1, 45 Stat. 1475; U.S.C. Title 28, Section 41 (5). (Tr. p. 4-31). The United States Circuit Court of Appeals for the Ninth Circuit has jurisdiction of this appeal from the Judgment of Dismissal of the said United States District Court for the Territory of Hawaii (Tr. p. 52-53) under the provisions of U.S.C. Title 28, Section 225 (Judiciary Code, Section 128).

Appellant has filed a timely Notice of Appeal (Tr. p. 55), Bond for Costs on Appeal (Tr. p. 55-58), Designation of Record on Appeal (District Court) (Tr. p. 59), Statement of Points Relied Upon on Appeal (District Court) (Tr. p. 60-61), and Statement of Points to be Relied Upon and Designation of Record to be Printed (Circuit Court of Appeals) (Tr. p. 77-80).

## STATEMENT OF THE CASE

(Note: The present plaintiff-appellant is the executor of the will of the deceased taxpayer plaintiff, Laura D. Sherman, and the present defendant-appellee is the executrix of the deceased collector defendant. For convenience and simplicity in stating and arguing the case, the deaths and substitution of parties will be ignored and the appellant will hereinafter be referred to as taxpayer or Laura D. Sherman.)

Under an agreement dated December 26, 1935, (Tr. p. 11-19) an irrevocable trust was created with George Sherman, husband of the taxpayer as Settlor, and Laura D. Sherman and the Hawaiian Trust Company, Limited, as trustees. Article I of the trust provides that the trustees shall pay to Laura D. Sherman, wife of the Settlor, during the remainder of her life all of the net income derived from said trust estate.

Frederick Dickson Nott, son of Laura D. Sherman, was divorced from Anna Adams Nott by a decree of divorce entered on April 28, 1936. (Pl. Exhibit A, Tr. p. 65-67). The decree ordered alimony of \$100 per month for the divorced wife so long as she should remain unmarried, and in addition \$75 per month each for the support and maintenance of Frederick Dickson K. Nott and Gretchen K. Nott (minor children of Frederick Dickson Nott and Anna Adams Nott) until the said minor children should have respectively achieved their majorities. The custody of the children was awarded to Anna Adams Nott.

By three separate documents dated April 16, 1936 (Tr. p. 19-25), Laura D. Sherman made assignments



of \$100 per month to Anna Adams Nott until death or remarriage, whichever is earlier, and of \$75 per month for each of the minor children until the respective child's death or majority, whichever is earlier, out of the income to which Laura D. Sherman was entitled from the said trust. These assignments were made because Frederick Dickson Nott, son of the taxpayer, did not have sufficient income himself to pay the amounts awarded in said decree of divorce and because Laura D. Sherman desired to assist him financially. (Tr. p. 45-46). On April 16, 1936, the date of said assignments, Frederick Dickson K. Nott was approximately ten years of age, Gretchen K. Nott was approximately nine years of age, Anna Adams Nott was approximately thirty-five years of age, and Laura D. Sherman was approximately sixty-seven years of age. (Tr. p. 46).

After the three assignments and pursuant thereto, the trustees paid the sum of \$3000 per year to Anna Adams Nott out of the net income of the said trust and the balance of the net income was paid to Laura D. Sherman. (Tr. pp. 46, 69).

In her income tax returns for the calendar years 1940 and 1941 Laura D. Sherman returned the entire net income of the said trust as income to her. (Tr. p. 47-48). Subsequently claims for refund were made on the ground that the income to her from the said trust had been overstated in each year in the amount of \$3000, such amount being the portion of the net income actually paid by the trustees to Anna Adams Nott pursuant to the three assignments. These claims for refund were rejected by the Commissioner of Internal

Revenue and this suit was instituted for the recovery of the alleged overpayments. (Tr. p. 48-49). The question here is whether all or any part of the income paid by the trustees to Anna Adams Nott by virtue of the said assignments during the years 1940 and 1941 is includable as part of the taxable gross income of taxpayer under the provisions of Sections 22(a), 161(a) and 162(b) of the Internal Revenue Code. Taxpayer contends that this in turn depends on whether the said assignments constituted a substantial disposition by the taxpayer of income producing property from which the income was derived. If it did, the income derived therefrom is no longer a part of the income of taxpayer under said provisions of the Internal Revenue Code.

The United States District Court for the Territory of Hawaii in its Special Findings of Fact and Conclusions of Law filed November 21, 1947 determined that the reversionary interest here of the taxpayer to the income assigned required the inclusion of the income assigned in the taxable gross income of the taxpayer. It is the contention of taxpayer that the said assignments were a substantial disposition of taxpayer's interest in the corpus of the trust and therefore that the taxpayer's ownership of the reversion is immaterial.

## SPECIFICATION OF ERRORS

### Specification of Error No. 1

The District Court of the United States for the District of Hawaii erred in making and entering its Special Findings of Fact and Conclusions of Law dated November 20, 1947, in the above cause.

### Specification of Error No. 2

The District Court of the United States for the District of Hawaii erred in rendering and entering Judgment of Dismissal dated February 17, 1948, in the above cause.

### Specification of Error No. 3

The evidence respecting the life expectancies of Laura D. Sherman, Anna Adams Nott, Frederick Dickson K. Nott and Gretchen K. Nott was relevant to show that the possibility of a reverter to Laura D. Sherman of the assigned interest was remote, and the District Court of the United States for the District of Hawaii erred in excluding as immaterial such evidence offered by the appellant. The evidence rejected was the facts respecting life expectancies contained in Paragraphs VIII, IX, X and XI of the Supplementary Stipulation and the grounds for objection are set forth in said stipulation in said paragraphs. Said evidence and objections are as follows:

#### "VIII.

"Said Anna Adams Nott, divorced wife of Frederick Dickson Nott, was born in Honolulu, Hawaii on April 28, 1901. On or about April 16, 1936 her age was approximately 34 years, 11 months. The Combined or Actuaries Experience Tables (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 30.93 years. The American Experience Table of Mortality (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 31.84 years. The



defendant objects to the admissibility in evidence of information showing the life expectancy of Anna Adams Nott as of on or about April 16, 1936, on the ground that such information is immaterial and irrelevant to the issue involved in this proceeding.

“IX.

“Said Frederick Dickson K. Nott, son of said Anna Adams Nott, was born in Honolulu, Hawaii, on November 22, 1925. On or about April 16, 1936 his age was approximately ten years, five months. The Combined or Actuaries Experience Tables (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 48.08 years. The American Experience Table of Mortality (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 48.46 years. The defendant objects to the admissibility in evidence of information showing the life expectancy of Frederick Dickson K. Nott as of on or about April 16, 1936, on the ground that such information is immaterial and irrelevant to the issue involved in this proceeding.

“X.

“Said Gretchen K. Nott, daughter of said Anna Adams Nott, was born in Honolulu, Hawaii on December 27, 1926. On or about April 16, 1936 her age was approximately nine years, four months. The Combined or Actuaries Experience Tables (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a per-

son of that age is 48.80 years. The American Experience Table of Mortality (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 49.14 years. The defendant objects to the admissibility in evidence of information showing the life expectancy of Gretchen K. Nott as of on or about April 16, 1936, on the ground that such information is immaterial and irrelevant to the issue involved in this proceeding.

#### “XI.

“Said Laura D. Sherman, mother of said Frederick Dickson Nott, was born on July 27, 1869. On or about April 16, 1936, her age was approximately 66 years 9 months. The Combined or Actuaries Experience Tables (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of a person of that age is 10.085 years. The American Experience Table of Mortality (printed in Wolfe, Inheritance Tax Calculations (2nd Ed.)) states that the life expectancy of person of that age is 10.13 years. The defendant objects to the admissibility in evidence of information showing the life expectancy of Laura D. Sherman as of on or about April 16, 1936, on the ground that such information is immaterial and irrelevant to the issue involved in this proceeding.” (Transcript pp. 72-74)

#### Specification of Error No. 4

Each of the three assignments dated April 16, 1936, constituted a transfer of a portion of the equitable interest of Laura D. Sherman in the corpus of the trust



dated December 26, 1935, and the District Court of the United States for the District of Hawaii erred in not so finding and deciding.

#### Specification of Error No. 5

Income paid to the assignees by virtue of said assignments was not taxable to Laura D. Sherman, and appellant is entitled to recover income taxes paid by Laura D. Sherman on account of said income, and the District Court of the United States for the District of Hawaii erred in not giving judgment for appellant accordingly.

#### Specification of Error No. 6

Each of the three assignments dated April 16, 1936 was a substantial disposition of the particular interest of Laura D. Sherman in the trust dated December 26, 1935, thus assigned, and the District Court of the United States for the District of Hawaii erred in finding and deciding that the income from such assigned interests was taxable to the assignor, of Laura D. Sherman.

#### Specification of Error No. 7

The reversionary interest of Laura D. Sherman in the interests transferred by the said three assignments was not substantial, particularly in relation to the interests transferred, and the District Court of the United States for the District of Hawaii erred in finding and deciding that the said reversionary interest was a substantial economic interest in the trust dated December 26, 1935.

## Specification of Error No. 8

The District Court of the United States for the District of Hawaii erred in finding and deciding that the retention of the reversionary interest by Laura D. Sherman in the interests assigned by her as aforesaid required the inclusion in her taxable gross income of income paid to the assignees by virtue of the said assignments.

## Specification of Error No. 9

The District Court of the United States for the District of Hawaii erred in finding and deciding that the facts of this case are controlled by the decision in *Harrison v. Schaffner*, 312 U.S. 79 rather than *Blair v. Commissioner*, 300 U.S. 5.

## SUMMARY OF ARGUMENT

*Blair v. Commissioner*, 300 U.S. 5, 57 S. Ct. 330, establishes the rule that assignment of income by a life beneficiary of income from a trust is a transfer of income producing property, and that the income derived therefrom is taxable to the assignee and not the assignor. *Harrison v. Schaffner*, 312 U.S. 579, 61 S. Ct. 759, places a limitation on this rule to the effect that a transfer which does not involve a substantial disposition of a trust property will not be recognized as shifting the burden of the tax from the assignor to the assignee. The factors which, taken collectively, normally establish the substantiality or insubstantiality of such a transfer are: (1) The period of the transfer, (2) whether the transfer is used to discharge a legal obligation of the taxpayer, and (3) whether it is a

device to avoid taxes. The transfers in the present case are substantial when tested on the basis of each and all of these factors.

## ARGUMENT

Section 22(a) of the Internal Revenue Code provides that " 'Gross Income' includes gains, profits, and income derived from \* \* \* \* interest, rent, dividends, securities or the transactions of any business carried on for gain or profit, or gains or profits, and income derived from any source whatever." By Sections 161-(a) and 162(b) of the Internal Revenue Code, the tax is laid upon the income "of any kind of property held in trust", and the income of a trust for the taxable year which is to be distributed to the beneficiaries is to be taxed to them "whether distributed to them or not". There is no doubt but that the income here in question is taxable to the beneficiary. What must be determined is whether taxpayer remained the beneficiary of the trust with respect to the interests assigned. That she was not the beneficiary under the circumstances of the present case within the meaning of the Revenue Laws has been determined by decisions of the United States Supreme Court and other Federal courts.

It has been long established that the assignment of income alone, such as the assignment of compensation for services, etc. (see *Lucas v. Earl*, 281 U.S. 111, 50 S. Ct. 241; *Burnet v. Leininger*, 285 U.S. 136, 52 S. Ct. 345; *Helvering v. Horst*, 311 U.S. 112, 61 S. Ct. 144; and *Helvering v. Eubank*, 311 U.S. 122, 61 S. Ct. 149) leaves such income taxable to the assignor. On the other hand, when income producing property is as-

signed, the income from such property is no longer taxable to the assignor. In *Blair v. Commissioner*, 300 U.S. 5, 57 S. Ct. 330, it was held that the assignment by a life beneficiary of a trust of a portion of the income receivable by him *constituted a transfer of the beneficiary's equitable interest in the property of the trust* and accordingly the income was held taxable to the assignee and not taxable to the assignor. The particular facts of the *Blair* case are as follows:

In the *Blair* case the life beneficiary of a trust assigned to one daughter an interest in the trust amounting to \$9000 out of the net income which the beneficiary was then or might be entitled to receive during his life. At about the same time like assignments of \$9000 per annum out of the income of the trust were made to a second daughter and son respectively. In later years these children were assigned additional interests and to another son other specified interests in net income.

The Supreme Court pointed out:

“The assignment of the beneficial interest is not the assignment of a chose in action but of the ‘right, title and estate in and to property’” (p. 13-14 of 300 U.S.)

and concluded that:

“the assignees thereby became the owners of the specified beneficial interests in the income, and that as to these interests they and not the petitioner were taxable for the tax years in question.” (p. 14 of 300 U.S.)

The analogy of the present case to the *Blair* case is so close that unless the rule of the *Blair* case has been



changed, the same result must logically follow.

Subsequent to the decision in the *Blair* case the Supreme Court decided *Helvering v. Clifford*, 309 U.S. 331, 60 S. Ct. 554. In that case a husband declared himself trustee of certain securities for the term of five years to pay to his wife the income accruing during that period but retained in himself the right to accumulate income and, with insignificant exceptions, complete control over the principal fund and the reversion of the corpus at the end of the term. The Supreme Court held, in short, that if the disposition of property is not substantial the tax authorities are justified in ignoring the disposition for tax purposes. It also held that such result was justified in that case.

With this background the case of *Harrison v. Schaffner*, 312 U.S. 579, 61 S. Ct. 759, was decided by the Supreme Court. In the *Schaffner* case the beneficiary of a trust executed irrevocable assignments of \$84,000 of the net income of the trust *for the year* 1930 to three children and under another assignment about a year later, \$54,000 of net income *of the year* 1931 to two of the same assignees and the surviving husband of the third. The court held the assignor taxable pointing out that (1) the "obvious purpose and effect" (p. 582 of 312 U.S.) of the assignment was the *avoidance of taxes*; (2) "that the gift by a beneficiary of a trust of some part of the income derived from the trust property for the period of a day, a month or a year involves no such substantial disposition of a trust property" (p. 582 of 312 U.S.) as to allow the assignor to escape the tax. The *Blair* case was distinguished on the ground that there there was a transfer of an "equi-



table interest in property for life effected by a gift for life of a share of the income of the trust" (p. 583 of 312 U.S.), while in the *Schaffner* case there was a "gift of the income or part of it for a period of a year" (p. 583 of 312 U.S.). The *Schaffner* case did not attempt to lay down a broad or general rule that assignors of income be taxable thereon. On the contrary, the hiatus between the *Blair* rule and the *Schaffner* rule was emphasized in the words,

"\* \* \* \* \* we leave it to future judicial decisions to determine precisely where the line shall be drawn between gifts of income producing property and gifts of income from the property of which the donor remains the owner, for all substantial and practical purposes. Cf. *Helvering v. Clifford*, *Supra*." (p. 583-4 of 312 U.S.)

It is clear from both the *Blair* and *Schaffner* cases that after the assignment of income producing property the income therefrom is no longer taxable to the assignor. However, the *Schaffner* case suspends the application of this rule pending the determination of whether the particular assignment of the beneficial interest in the trust is one which results in a substantial transfer of income-bearing property. If the assignment is found to have resulted in a substantial transfer of income-bearing property, the income therefrom is no longer taxable to the assignor. This determination, as illustrated by the *Blair*, *Clifford* and *Schaffner* cases and succeeding cases hereinafter referred to, turns upon several conditions, none of which alone is necessarily determining but which when taken collectively provide the basis for characterizing the transfer as substantial or insubstantial, as effective or

non-effective and finally concluding upon whom the burden of tax will fall. These conditions or determining factors for the most part are as follows: (1) The period of the transfer, (2) whether the income assigned is used to discharge a legal obligation of the taxpayer, and (3) whether it is a device to avoid taxes.

In the matter of period of transfer, three cases have involved assignments for a single year: *Huber v. Helvering*, 117 F. (2d) 782 (Court of Appeals, D.C.) decided prior to *Schaffner*, *Schaffner*, and *Hyman v. Nunan*, 143 F. (2d) 425 (CCA-2), decided subsequent to *Schaffner*. These cases held the income taxable to the assignor. Two cases decided subsequent to *Schaffner* which have involved assignments for longer than a single year have held the assignee taxable and the assignor not. Thus, in *Mahaffey v. Helvering*, 140 F. (2d) 879 (CCA-8), the beneficiary assigned trust income to his mother, then 76, for her life, and in *Belknap v. Glenn*, 55 Supp. 631 (D.C. W.D. Ky.), where the assignment was for life. Of the assignments made by Laura D. Sherman, one is to the assignee for life or until remarriage, and two are for periods of approximately ten and eleven years being until the children reach majority, or until their prior deaths. That the assignments may terminate prior to the deaths of the assignees is not significant in the present case since by the terms of the instrument such determination is upon contingencies *beyond any control of the assignor*. The assignments made by Laura D. Sherman have nothing in common with the assignments in the *Huber*, *Schaffner*, and *Hyman* cases, so far as the time factor is concerned. The periods of her assignments illustrate the difference in her purpose

from the purposes of the assignments in those cases.

This is especially true in view of the respective ages of Mrs. Sherman, Mrs. Nott and the two children at the time of the assignments. With respect to the \$100 assignment for the life of Anna Adams Nott, Mrs. Sherman was approximately 67 and Mrs. Nott was approximately 35 at the time of the assignment. It is obvious that all reasonable persons would expect Mrs. Nott to outlive Mrs. Sherman and expectancy tables would of course have borne this out. Accordingly that assignment was for all practical purposes the equivalent of an assignment for the life of Mrs. Sherman, thus demonstrating the closeness of the analogy to the *Blair* case. With respect to the assignments for the benefit of the two children, the transfers were for periods of over ten and eleven years respectively. At age 67 it was to be expected that this was approximately the life expectancy of Mrs. Sherman so that again for practical purposes it was the substantial equivalent of a transfer for the life of Mrs. Sherman, and, of course, expectancy tables would again have pointedly demonstrated this fact. There is no implication that the technical possibility of reversion to Mrs. Sherman was retained by her for the purposes of control. The periods of the assignments were tailored to fit exactly the requirements of the said divorce decree. In the *Schaffner* case the implication was strong from the facts that the assignor was attempting to control and yet avoid taxes according to her annual convenience. Can it fairly be said that Mrs. Sherman's assignments can be similarly characterized?

Further with respect to the period of the transfer,



can a period of ten years be characterized as of short duration? In the *Clifford* case the term was five years accompanied by many other factors not present here. On the other hand, the income of a ten year trust has been held to be not taxable to the grantor. *Commissioner v. Jonas*, 122 Fed (2d) 169 (CCA-2).

With respect to the factor of whether the income was used to discharge a legal obligation of the assignor, it is clear that Mrs. Sherman had no legal obligation to provide for the support and maintenance of her son's children or to pay alimony to his divorced wife.

No lengthy explanation is necessary to point out that the present assignment was not an attempt to evade taxes, and the District Court found accordingly. (Tr. p. 46). It was a well intentioned effort to assist a financially embarrassed son to meet his alimony obligations (Tr. p. 45-46, 39-40); a highly practical solution to a practical problem other than tax savings.

That the rule of the *Blair* case is still good law cannot be disputed as it has been followed in subsequent cases such as *Belknap* and *Mahaffey*, and the Supreme Court paid homage to it in deciding the *Schaffner* case.

The closest case on its facts to the present case since the decision in the *Schaffner* case is *Leonard Farkas v. Commissioner*, 8 T.C. 1351. The decision in this case was against the taxpayer, but there was a strong dissent in the Tax Court and an appeal is presently pending before the United States Circuit Court of Appeals for the Fifth Circuit. In the *Farkas* case, the taxpayer was the recipient for life of one-eighth of the income of a trust created by his father. Taxpayer assigned

his right to receive the income of this trust to his brother in trust to distribute the same among various named relatives. The assignment was for a period of ten years, or until the prior death of the brother. Taxpayer was fifty-three years old at the time, the brother fifty-eight. The Tax Court held in effect that only an assignment of the income for the life of the taxpayer would result in this income being taxed to the assignee, the retention of any reversionary interest in the assignor being sufficient to bring the case within the rationale of the *Schaffner* case. The dissent (8 T.C. at pp. 1358-1359) in the *Farkas* case recognized this fallacy, as follows:

“ARUNDELL, J., dissenting: As in *Blair v. Commissioner*, 300 U.S. 5, the petitioner here was a life beneficiary of a testamentary trust. That gave him an equitable interest in the corpus. See also *Irwin v. Gavit*, 268 U.S. 161. His equitable interest in the corpus, in the absence of a valid restraint upon alienation, was assignable in whole or in part. Here, as in *Blair*, the petitioner assigned a part of his interest to others, though here, through the medium of a second trust; and a state court has held the assignment valid. (Indeed, if it had been otherwise, the petitioner's interest would have been forfeited according to the express terms of his father's will, and then there could be no basis whatever for taxing the income to him.)

“In such a case, as distinguished from the assignment of compensation for services, past, present, or future, *Blair* holds that the taxation of income is predicated upon ownership of the property; hence the tax falls on the assignee. Thus it would seem that, in the absence of a change in the rule, the analogy of the instant case to *Blair* is



so close that the result logically should be the same.

“We know, however, that the impact of *Helvering v. Clifford*, 309 U.S. 331, has forced a modification of the rule with respect to the taxation of income from property; in short, if the disposition of the property is not substantial, the income will be taxed as if no disposition at all had been made. It is therefore necessary to evaluate the present case with that principle in mind, for it can not be doubted that the intervening *Clifford* decision very largely influenced the result in *Harrison v. Schaffner*, 312 U.S. 579. The rationale of both cases is much the same. *Schaffner* holds that the ‘gift by a beneficiary of a trust of some part of the income derived from the trust property for the period of a day, a month, or a year involves no such substantial disposition of the trust property’ as to allow the donor to escape the tax.

“Tested in the light of the *Clifford* principle, can it fairly be said that the petitioner has not made a *substantial* disposition of his interest in the trust property? Unlike *Clifford*, petitioner did not make himself the trustee, but chose an independent trustee. Neither did he retain any powers or control over the property. He was a bachelor and was in no way obligated to support the beneficiaries of the trust—his adult brothers and sisters and their children. Nor did he and the beneficiaries comprise either an intimate family group or one economic unit. Finally, it is clear that the mere nonmaterial satisfaction of making gifts to his brothers and sisters is not alone sufficient to require taxing the income to him. *Helvering v. Stuart*, 317 U.S. 154.

“It is obvious that the only *Clifford* factor present in this case is the ‘short duration of trust’—there five years, here ten. But I know of no case

where, that being the only factor present, any court has held the income of a ten-year trust taxable to the grantor. The respondent has cited none. On the other hand, the Second Circuit held exactly the contrary in *Commissioner v. Jonas*, 122 Fed. (2d) 169.

"The conclusion of the majority that this case is controlled by *Schaffner* extends the scope of that case beyond anything I think the Supreme Court there decided or intended, and it makes of *Blair* practically a nullity. I respectfully dissent.

"VAN FOSSAN, BLACK, and LEECH, JJ., agree with this dissent."

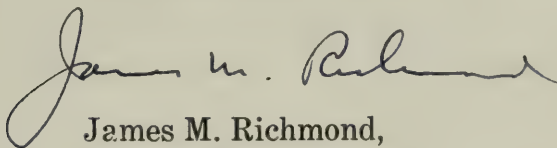
All the errors specified stem from a fundamental misconception of the holding in the *Schaffner* case. The District Court apparently proceeded on the theory that the *Schaffner* case laid down a broad rule which requires that assignors of trust income be taxable thereon if the assignor retains a reversionary interest in the property assigned. Particular emphasis was laid on the termination of the assignments on the contingencies of death or remarriage, and in line with the same thinking, evidence concerning life expectancies which pointedly demonstrated the substantiality of the transfers was excluded as immaterial.

Summing up our argument as to the errors of the Court below the law is clear and undisputed that where there is an effective assignment of income producing property, the income therefrom is not taxable to the assignor. The assignments here were *substantial* dispositions within the rationale of the *Clifford*, *Schaffner* and other cases and therefore effective as such. Consequently, Laura D. Sherman in assigning stipulated

sums of income payable from the income of the trust to the assignee, effected an assignment of rights in and to the corpus of the trust under the *Blair* rule and as to the income derived from these beneficial interests, the assignees are taxable and Laura D. Sherman is not. Therefore, Laura D. Sherman overpaid her income taxes for the years 1940 and 1941 and her executor is entitled to recover the amount thus overpaid.

It is requested that the Judgment of Dismissal of the United States District Court for the Territory of Hawaii be reversed and set aside, and that court directed to enter judgment for plaintiff accordingly.

Respectfully submitted,

A handwritten signature in dark ink, appearing to read "James M. Richmond". The signature is fluid and cursive, with a large initial "J" and a long, sweeping underline.

James M. Richmond,  
Attorney for Appellant,  
Hawaiian Trust Company, Limited,  
Executor of the Will of Laura  
D. Sherman, Deceased.



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In the United States Court of Appeals  
for the Ninth Circuit

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No. 11909

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HAWAIIAN TRUST COMPANY, LIMITED, *Executor of the  
Will of Laura D. Sherman, Appellant*

v.

AGNES M. KANNE, *Executrix under the Will of Fred H.  
Kanne, Deceased, Appellee*

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On Appeal from the District Court of the United States for the  
Territory of Hawaii

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BRIEF FOR THE APPELLEE

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FILED

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*Assistant Attorney General.*

SEP 7 1948

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## INDEX

	Page
Opinion below .....	1
Jurisdiction .....	1
Question presented .....	2
Statutes and Regulations involved .....	2
Statement .....	3
Summary of argument .....	8
Argument: The life beneficiary remained taxable with respect to the assigned income .....	9
A. The assignments were of future income only, and the as- signor's reversionary interest constituted a substantial eco- nomic interest in the trust .....	9
B. The decision in the <i>Blair</i> case is not opposed to the Collec- tor's position here .....	18
C. The taxing statute fixes accountability for the tax upon the taxpayer because of her status as life beneficiary of the trust .....	22
Conclusion .....	24
Appendix .....	25

## CITATIONS

### CASES:

<i>Belknap v. Glenn</i> , 55 F. Supp. 631 .....	18
<i>Bing v. Bowers</i> , 22 F. 2d 450, affirmed, 26 F. 2d 1017 .....	22
<i>Blair v. Commissioner</i> , 300 U. S. 5 .....	8, 12
<i>Burnet v. Leininger</i> , 285 U. S. 136 .....	10
<i>Burnet v. Wells</i> , 289 U. S. 670 .....	10
<i>Commissioner v. Jonas</i> , 122 F. 2d 169 .....	16
<i>Corliss v. Bowers</i> , 281 U. S. 376 .....	10, 21
<i>DuPont v. Commissioner</i> , 289 U. S. 685 .....	10
<i>Farkas v. Commissioner</i> , 8 T. C. 1351 .....	17
<i>Harrison v. Schaffner</i> , 312 U. S. 579 .....	8, 10
<i>Helvering v. Clifford</i> , 309 U. S. 331 .....	10
<i>Helvering v. Eubank</i> , 311 U. S. 122 .....	8, 10
<i>Helvering v. Horst</i> , 311 U. S. 112 .....	8, 9
<i>Huber v. Helvering</i> , 117 F. 2d 782 .....	18
<i>Hyman v. Nunan</i> , 143 F. 2d 425 .....	18
<i>Lucas v. Earl</i> , 281 U. S. 111 .....	10
<i>Mahaffey v. Helvering</i> , 140 F. 2d 879 .....	18
<i>Poe v. Seaborn</i> , 282 U. S. 101 .....	23
<i>Reinecke v. Smith</i> , 289 U. S. 172 .....	10

## STATUTES:

	Page
Internal Revenue Code:	
Sec. 22 (26 U.S.C. 1946 ed., Sec. 22) -----	25
Sec. 161 (26 U.S.C. 1946 ed., Sec. 161) -----	25
Sec. 162 (26 U.S.C. 1946 ed., Sec. 162) -----	26

## MISCELLANEOUS:

Treasury Regulations 103:	
Sec. 19.22(a)-1 -----	27
Sec. 19.161-1 -----	27
Sec. 19.162-1 -----	29

**In the United States Court of Appeals  
for the Ninth Circuit**

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No. 11909

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HAWAIIAN TRUST COMPANY, LIMITED, *Executor of the  
Will of Laura D. Sherman, Appellant*

v.

AGNES M. KANNE, *Executrix under the Will of Fred H.  
Kanne, Deceased, Appellee*

---

**On Appeal from the District Court of the United States for the  
Territory of Hawaii**

---

**BRIEF FOR THE APPELLEE**

---

**OPINION BELOW**

The opinion of the District Court (R. 41-51) is reported in 76 F. Supp. 224.

**JURISDICTION**

This appeal involves federal income taxes for the calendar years 1940 and 1941. The taxes in dispute were paid by Laura D. Sherman, the taxpayer, as follows: \$4,274.57 with respect to the taxable year 1940, in installments of \$1,068.65 on March 15, 1941, \$1,068.65 on June 14, 1941, \$1,068.64 on September 12, 1941, and \$1,068.63 on December 12, 1941 (R. 47); and \$6,046.15 with respect to the taxable year 1941, in installments of

\$1,511.54 on March 16, 1942, \$1,511.54 on June 13, 1942, \$1,511.54 on September 14, 1942, and \$1,511.53 on December 15, 1942 (R. 48).<sup>\*</sup> Claim for refund of \$969.65 of the 1940 income tax and claim for refund of \$1,434.81 of the 1941 income tax were filed on March 14, 1944, by Laura D. Sherman, since deceased, and rejected. (R. 48-49.) Within the time provided in Section 3772 of the Internal Revenue Code and on October 30, 1945, the taxpayer brought an action in the District Court for recovery of the taxes alleged to have been overpaid as stated in the claims for refund. (R. 2, 9, 10.) Jurisdiction was conferred on the District Court by Section 24, subsections Fifth and Twentieth of the Judicial Code, as amended. The judgment was entered on February 18, 1948, in favor of the Collector, dismissing the appellant's action with costs. (R. 52-53.) Thereafter, within three months the appellant's notice of appeal was filed on March 17, 1948. (R. 55.) The jurisdiction of this Court is invoked under the provisions of 28 U. S. C., Sec. 1291.

#### QUESTION PRESENTED

Whether Laura D. Sherman, life beneficiary of an *inter vivos* trust created by her husband in 1935, is taxable on that part of the income thereof in the years 1940 and 1941 which was paid to her son's divorced wife for her support and the support of her two minor children in accordance with irrevocable assignments executed by Mrs. Sherman in 1936.

#### STATUTES AND REGULATIONS INVOLVED

The applicable statutes and Regulations involved will be found in the Appendix, *infra*.

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<sup>\*</sup> Thereafter, on August 5, 1944, Mrs. Sherman paid to Collector Kanne a deficiency of \$90 in income tax for the year 1941, plus interest thereon of \$12.91, or a total of \$102.91, which is not involved in this controversy. (R. 48.)



**STATEMENT**

The pertinent facts, sufficient for the purposes herein, were found by the District Court substantially as follows (R. 41-49): Laura D. Sherman, now deceased, a resident of the Territory of Hawaii, brought this action to recover federal income taxes for the calendar years 1940 and 1941 alleged to have been illegally assessed and collected by Fred H. Kanne, now deceased, who was then the Collector of Internal Revenue for the District of Hawaii. Laura D. Sherman died on June 11, 1947. The Hawaiian Trust Company, Limited, of Honolulu, having qualified and been confirmed as executor of her will on July 15, 1947, was substituted as plaintiff appellant herein on July 22, 1947. (R. 36-38.) Fred H. Kanne died on December 24, 1946. His widow, Agnes M. Kanne, of Honolulu, having qualified and been confirmed as executrix of his will on February 4, 1947, was substituted as defendant appellee herein on March 6, 1947. (R. 34-36, 49.)

The facts were stipulated and admitted into evidence except those facts stated in the supplementary stipulation relating to the life expectancy of Anna Adams Nott, Frederick Dickson K. Nott, Gretchen K. Nott, and Laura D. Sherman, which were not admitted in evidence, on the ground that such information was wholly immaterial in the case. (R. 41.)

The deceased taxpayer, Laura D. Sherman, was the sole life beneficiary and co-trustee of an irrevocable *inter vivos* trust created by her husband on December 26, 1935, in which it was provided that all of the net income derived from the trust estate should be paid to her during her lifetime. (R. 42.)

*In anticipation of the divorce of her son, Frederick Dickson Nott, from his wife, Anna Adams Nott, which was accomplished by a decree of divorce entered on April 28, 1936, Laura D. Sherman, by separate docu-*

ments each dated *April 16, 1936*, made assignments of \$100 a month to Anna Adams Nott until death or remarriage, whichever is earlier, and \$75 a month for each of the minor children until the respective child's death or majority, whichever is earlier, out of the income to which she (Laura D. Sherman) was entitled from the trust set up by her husband. (R. 42-43.) These assignments of income were made because Frederick Dickson Nott, the taxpayer's son, did not have sufficient income himself to pay the amounts awarded in the divorce decree which had ordered alimony of \$100 a month to his divorced wife so long as she should remain unmarried, and in addition \$75 a month each for the support and maintenance of his two minor children until the minors should have respectively attained their majorities. Laura D. Sherman was prompted to make these assignments of income by a desire to assist her son financially and not for tax-avoidance purposes. (R. 42, 45-46.)

The pertinent part of the assignment to Anna Adams Nott read as follows (R. 43-44) :

Now Therefore the premises considered, the undersigned, Laura D. Sherman, hereinafter referred to as the assignor, does hereby assign, transfer and set over unto Anna Adams Nott, hereinafter referred to as the assignee, the sum of One Hundred Dollars (\$100.00) a month from the income to which the assignor now is or shall be entitled to receive as life beneficiary under the terms and provisions of that certain unrecorded trust deed dated December 26, 1935, executed by George Sherman as settlor and the assignor and Hawaiian Trust Company, Limited, an Hawaiian corporation, as trustees, until the death or remarriage of the assignee whichever event shall first occur and upon the occurrence of either of said

events this assignment shall become inoperative and shall be of no further force or effect.

The Hawaiian Trust Company, Limited, co-trustee under said trust deed, is hereby empowered and directed to pay from the assignor's income, as aforesaid, the sum of One Hundred Dollars (\$100.00) a month to the said assignee, the first of such payments to be made on the 1st day of May, 1936, and a like sum on the 1st day of each and every month thereafter until the death or remarriage of said assignee, whichever event shall first occur, and upon the occurrence of either of such events of which said Hawaiian Trust Company, Limited, shall have strict and exact proof, all payments shall cease and determine.

The pertinent part of the assignments for each of the minor children read as follows (R. 44-45):

Now Therefore in consideration of the premises and of the promise of the assignee hereinafter contained the assignor does hereby assign, transfer and set over unto the assignee the sum of Seventy-Five Dollars (\$75.00) a month from the income to which the assignor now is or shall be entitled to receive as life beneficiary under the terms and provisions of that certain unrecorded trust deed dated December 26, 1935, executed by George Sherman as settlor and the assignor and Hawaiian Trust Company, Limited, an Hawaiian corporation, as trustees, which sum is to be used by the assignee solely for the support, education and maintenance of said minor during his minority provided, however, and this assignment is upon this express condition, that upon the occurrence of any of the following events this assignment shall become



inoperative and all payments authorized to be made herein shall cease and determine, such events being:

- (1) Upon the death of said minor or the assignee;
- (2) Upon the said minor attaining his majority under the laws of the jurisdiction in which said minor is then living;

The Hawaiian Trust Company, Limited, co-trustee under said trust deed, is hereby empowered and directed to pay from the assignor's income, as aforesaid, the sum of Seventy-Five Dollars (\$75.00) a month to the said assignee, the first of such payments to be made on the 1st day of May, 1936, and a like sum on the 1st day of each and every month thereafter until the occurrence of any one or more of the above mentioned events and upon the occurrence of any of such events (of which said Hawaiian Trust Company, Limited, shall have strict and exact proof) all payments shall cease and determine.

On April 16, 1936, the date of the assignments, Frederick Dickson K. Nott was approximately ten years of age, Gretchen K. Nott was approximately nine years of age, Anna Adams Nott was approximately thirty-five years of age, and Laura D. Sherman was approximately sixty-seven years of age. (R. 46.)

Pursuant to the assignments, the trustees of the Sherman trust paid out of the net income thereof to Anna Adams Nott the total sum of \$1,200 during each of the calendar years 1940 and 1941 for her support, and also paid out of the net income of the trust to Anna Adams Nott an additional total sum of \$1,800 during each of the calendar years 1940 and 1941 for the support and maintenance of her two minor children. (R. 46.)

Anna Adams Nott and her two children, Frederick Dickson K. Nott and Gretchen K. Nott, are presently surviving and reside in the State of Washington where they have resided since 1942. Prior to April 16, 1936, these individuals each resided in Hawaii until December 5, 1941, when they departed from Hawaii for the State of Washington. Under the laws of the Territory of Hawaii the age of majority is twenty years, whereas under the laws of the State of Washington the age of majority is twenty-one years. (R. 47.)

During the calendar year 1940 the trustees of the Sherman trust paid to Laura D. Sherman the total sum of \$6,332.42 of the net income of the trust estate, and she included in her federal income tax return for that year the sum of \$9,332.40, representing the entire amount of the net income of the trust for that year. During the calendar year 1941, the trustees paid Laura D. Sherman the total sum of \$7,598.98 of the net income of the trust estate, and she included in her federal income tax return for that year \$10,598.98, representing the entire amount of the net income of the trust for that year. (R. 42, 47, 48.)

The District Court held that the gifts of income made by the three assignments dated April 16, 1936, to the taxpayer's daughter-in-law and grandchildren, while substantial in amounts, were, respectively, upon the happening of any one of the conditions provided in the assignments brought to an end, and the respective assignment thereupon terminated, and that Laura D. Sherman, the assignor taxpayer, retained the *entire* reversionary interest in the income so assigned, which reversion, representing as it does, a substantial economic interest in the Sherman trust dated December 26, 1935, definitely requires the inclusion of the assigned income as part of the taxable gross income of the assignor under the provisions of Section 22(a) of



the Internal Revenue Code and the applicable Treasury Regulations promulgated thereunder, and brings the taxability of such assigned income within the rationale of the Supreme Court's opinion in the case of *Harrison v. Schaffner*, 312 U. S. 579, and excludes it from the rationale of that Court's opinion in the case of *Blair v. Commissioner*, 300 U. S. 5, relied upon by the taxpayer. (R. 50.)

#### SUMMARY OF ARGUMENT

This case is ruled by *Harrison v. Schaffner*, 312 U. S. 579. Without relinquishing her life estate, the taxpayer simply deflected part of her income therefrom for a short period not co-extensive with her life to her former daughter-in-law and grandchildren. The *Schaffner* case and the cases of *Helvering v. Horst*, 311 U. S. 112, and *Helvering v. Eubank*, 311 U. S. 122, as well as other decisions of the Supreme Court, make it clear that such an assignment does not relieve the assignor of tax liability. *Blair v. Commissioner*, 300 U. S. 5, is not opposed. There the owner of a life estate assigned *for the duration of his life* a specified portion of the income to which he was entitled, and the Supreme Court held he was not taxable on the income thus paid to the assignees. But the decision in this case rested on the theory that the assignor had disposed, not merely of his right to income, but also of his *entire* life interest. If the *Blair* case be regarded as standing for more than this, it would be inconsistent with other cases involving assignments of income. Thus, if the taxpayer in the *Horst* case, *supra*, had transferred the bonds in trust for himself, and then assigned a portion of the income therefrom to his son for a short period, it could be argued that the *Blair* case would not have required a different result. But since there is no magic in the trust device, the crucial issue is whether the taxpayer had parted with an underlying interest out of which

the income flowed. The taxpayer here, unlike the assignor in the *Blair* case, did not part with her underlying property interest, i. e., her life estate, and therefore continued to remain liable with respect to the entire trust net income whether it was actually received by her or deflected to the assignees. In substance, the assignments are powers of attorneys to receive the income to which the taxpayer "now is or shall be entitled to receive." When the assignees collect under these instruments, they do not collect their own income. By the terms of the instruments they are to collect the income due to the taxpayer.

#### ARGUMENT

#### **The Life Beneficiary Remained Taxable with Respect to the Assigned Income**

##### **A. The assignments were of future income only, and the assignor's reversionary interest constituted a substantial economic interest in the trust**

The taxpayer was a life beneficiary of a trust. Without in any way relinquishing her life interest therein, she carved out a portion of the yearly income thereof to which she was entitled and directed the trustees of that trust (of which she was also a co-trustee) to pay to Anna Adams Nott for her support and the support of the taxpayer's minor grandchildren stated amounts monthly out of the income until the happening of any one of the conditions provided in the assignments, whereupon the assignments terminated. Thus she retained the entire reversionary interest in the income so assigned upon the happening of the conditions which terminated the assignments. Accordingly, we submit that the assignments did not effectively relieve the assignor of liability for the tax on such assigned income.

Like the owner of the coupon bonds in *Helvering v. Horst*, 311 U. S. 112, the taxpayer in the instant case

simply reallocated a portion of her future income within the family group without relinquishing her interest in the underlying trust estate from which the income was separated. In the *Horst* case the property was bonds; here the property was a life estate in a trust. We believe there are no essential differences in the two cases.

The rule in the *Horst* case and its companion case of *Helvering v. Eubank*, 311 U. S. 122, followed established principles. See *Lucas v. Earl*, 281 U. S. 111; *Burnet v. Leininger*, 285 U. S. 136; *Helvering v. Clifford*, 309 U. S. 331; *Reinecke v. Smith*, 289 U. S. 172, 177; *Harri-son v. Schaffner*, 312 U. S. 579. Cf. *Corliss v. Bowers*, 281 U. S. 376; *DuPont v. Commissioner*, 289 U. S. 685; *Burnet v. Wells*, 289 U. S. 670. And the facts in the instant case make the application of these principles particularly appropriate here, especially the rule laid down in the *Schaffner* case.

In every real sense, we believe the taxpayer here exercised control over the flow of the income in question. She directed the trustees of the Sherman trust, of which she was both a co-trustee and the sole beneficiary, to pay from her income stated amounts each month to her daughter-in-law for her daughter-in-law's support and for the support of her grandchildren until the occurrence of designated events, all of which could have happened before the taxpayer's death, and upon the happening of any one of which events, all payments of income to the particular assignee were to cease and terminate. Thus, Laura D. Sherman, as assignor, retained the entire reversionary interest in the income so assigned.

Not only did she retain such interest in the income, but as co-trustee with the Hawaiian Trust Company, the appellant herein, Mrs. Sherman had power under paragraph 5 of the Sherman trust indenture (R. 15-16) to manage and control the property included in the trust



estate, to sell it, to exchange it, and to reinvest the proceeds of the sale thereof. Thus, by manipulating the disposition of the trust estate, the trustees could effectively limit the income thereof, and if for some reason the income of the trust dropped below the \$3,000 payable to the assignees pursuant to the assignments of Laura D. Sherman, the assignees were without recourse to require the trustees of the Sherman trust to invade principal to make up any deficiency in income or change the trust investments. Moreover, paragraph 13 of the trust deed (R. 18) clearly shows that it was the settlor's intention that his wife, Laura D. Sherman, should not have any interest whatsoever in the principal of the trust estate. That paragraph of the trust indenture provides that no amendment thereof shall authorize the payment or application of any part of the principal of the trust estate to or for the benefit of the settlor's wife, Laura D. Sherman. We think these circumstances demonstrate that the assignees acquired no interest in the principal of the trust, but merely a right to receive a share of the income, if any, up to \$3,000 a year until the happening of the events which terminated their interest in the income thereof.

We think the present case is controlled by *Harrison v. Schaffner*, *supra*, where the life beneficiary of a trust assigned to her children specified amounts in dollars from the income of the trust for the year following the assignment, and repeated the ritual the following year. The respondent in that case rested his case on technical distinctions affecting the conveyancing of equitable interests (pp. 580-581) arguing that by the assignment of trust income, the assignee acquires an equitable right to an accounting by the trustee which, for many purposes, is treated by courts of equity as a present equitable estate in the trust property so that each assignee is a donee of an interest in the trust property for the term

of the assignment, and thus the recipient of income from his own property which is taxable to him rather than to the donor. But the Supreme Court in the *Schaffner* case remarked as it had theretofore done in *Lucas v. Earl*, 281 U. S. 111, 114, that the operation of the statutes taxing income is not dependent upon such attenuated subtleties, and proceeded to decide the issue in accordance with the reasoning of its opinions in *Corliss v. Bowers*, *supra*; *Lucas v. Earl*, *supra*, *Helvering v. Horst*, *supra*; *Helvering v. Eubank*, *supra*, and *Helvering v. Clifford*, *supra*, stating that these decisions were controlling in the *Schaffner* case. Distinguishing *Blair v. Commissioner*, 300 U. S. 5, upon which the taxpayer relied, the Court said (pp. 582-583):

We think that the gift by a beneficiary of a trust of some part of the income derived from the trust property for the period of a day, a month or a year involves no \* \* \* substantial disposition of the trust property as to camouflage the reality that he is enjoying the benefit of the income from the trust of which he continues to be the beneficiary, \* \* \*. Even though the gift of income be in form accomplished by the temporary disposition of the donor's property which produces the income, the donor retaining every other substantial interest in it, we have not allowed the form to obscure the reality. Income which the donor gives away through the medium of a short term trust created for the benefit of the donee is nevertheless income taxable to the donor. *Helvering v. Clifford*, *supra*; *Hormel v. Helvering*, \* \* \* [312 U. S. 552]. We perceive no difference, so far as the construction and application of the Revenue Act is concerned, between a gift of income in a specified amount by the creation of a trust for a year, see *Hormel v. Helvering*, *supra*, and the assignment by the benefi-



ary of a trust already created of a like amount from its income for a year.

Continuing the Court said (p. 583):

Nor are we troubled by the logical difficulties of drawing the line between a gift of an equitable interest in property for life effected by a gift for life of a share of the income of the trust and the gift of the income or a part of it for the period of a year as in this case. "Drawing the line" is a recurrent difficulty in those fields of the law where differences in degree produce ultimate differences in kind. \* \* \*. It is enough that we find in the present case that the taxpayer, in point of substance, has parted with no substantial interest in property other than the specified payments of income which, like other gifts of income, are taxable to the donor.

The District Court which tried the present case followed the reasoning of the Supreme Court's opinion in the *Schaffner* case and concluded that Laura D. Sherman the assignor and taxpayer in the instant case retained the entire reversionary interest in the assigned income, and that this reversion, representing as it does a substantial economic interest in the Sherman trust, requires the inclusion of the assigned income as part of the taxable gross income of the assignor. (R. 50.) But the taxpayer argues that while each of the assignments was a substantial disposition of the particular interest of Mrs. Sherman in the trust dated December 26, 1935, the reversionary interest of Mrs. Sherman in the interests so transferred was not substantial, and that the trial court erred in finding and deciding that her reversionary interest was a substantial economic interest in that trust. (Br. 9.) And, at the conclusion

of its arguments, the taxpayer again repeats the argument that the assignments were substantial. (Br. 20-21.) Now, we submit, if the assignments of income were substantial dispositions, it must follow *a fortiori* that the right to have this income back at the termination of the assignments constituted a substantial economic reversionary interest. By the same token, if these assignments effected a substantial economic equitable interest in the principal of the trust, then the assignor's reversionary interest likewise constituted a comparable economic interest. So, we submit that the District Court was correct in finding and deciding that Mrs. Sherman's reversionary interest was a substantial economic interest in that trust. Accordingly, we believe the District Court's decision should be affirmed.

The taxpayer's position seems to stem from the erroneous premises that the termination of the assignments was dependent upon contingencies beyond any control of the assignor, and that the fact that the assignments could terminate prior to the deaths of the assignees is not significant. (Br. 15.) That reasoning ignores the important fact that, by providing for the termination of the assignments upon such contingencies, the assignor indisputably expressed her intention not to dispose of her full life interest in the trust. Even if it were reasonable to assume that Mrs. Sherman would probably predecease the assignees (Br. 16), we think that such a probability is immaterial to the determination of the issue here involved. The important fact is that by the language used to designate the periods of each assignment Mrs. Sherman did not in any way indicate an intention to dispose of her entire life estate or to dispose of any interest in the trust co-extensive with her own life. That she did not so intend is manifested by the fact, as the taxpayer admits (Br. 16) that the assignments were tailored to fit exactly the require-

ments of the divorce decree. Since the events so designated could have happened, and in the case of the children apparently did happen before Mrs. Sherman died, we submit that the taxpayer's argument that (Br. 16)—

for practical purposes it was the substantial equivalent of a transfer for the life of Mrs. Sherman, \* \* \*

is just plain sophistry. An inspection of the instruments of assignment will disclose that Mrs. Sherman assigned only a part of the income otherwise distributable to her for periods less than the duration of her life, retaining the right to have that income at the termination of the designated periods. She merely assigned a *fixed amount* monthly from the income that she was entitled to receive. These assignments, being for periods less than the duration of the assignor's life and *not constituting her entire interest in the trust*, clearly did not represent a substantial interest *in the trust property* other than the specified payments of income which, like other gifts of income, are taxable to the donor. *Harrison v. Schaffner*, 312 U. S. 579, 583. The possibility that she might die before the happening of the termination events provided in the instruments certainly did not impart to the assignments characteristics which made them substantially equivalent to transfers for Mrs. Sherman's life. If it is proper to regard Mrs. Sherman's assignments as transfers for her life, then by the same token, the yearly assignments in the *Schaffner* case should have been so regarded because even for such a short period the assignor could have died before the expiration of the year. But as the Supreme Court did not so regard those assignments in the *Schaffner* case, there is no logical reason for regarding Mrs. Sherman's assignments as made for her life. In every case where a life beneficiary of a trust makes an assignment

of income, it must terminate with the assignor's death. It would open the door to tax avoidance if such an absurd interpretation were placed upon all assignments of income by life beneficiaries. The Supreme Court's opinion in the *Schaffner* case effectually closes the door to such legal chicanery.

Neither does the possibility that these assignments might extend for a period of ten years exclude them from being categorized as assignments of short duration. The taxpayer's argument (Br. 16-17) appears to be predicated on the erroneous premise that the period of the assignment made by Mrs. Sherman was for a period of ten years, and cites in support of its argument the case of *Commissioner v. Jonas*, 122 F. 2d 169 (C. C. A. 2d), which involved the taxability of the income of two trusts, <sup>under the</sup> were each limited to a period of ten years, but which were further extended prior to expiration from time to time. The *Jonas* case is clearly distinguishable on its facts from the instant case. That case involved the taxability to the settlor of the income of two trusts, which was payable to her two sons. The instant case does not involve the taxability of trust income to the settlor, but the taxability to the life beneficiary of trust income, part of which she assigned to others for limited periods less than for the duration of her life. Unlike the taxpayer in the *Jonas* case, Mrs. Sherman was a co-trustee of the trust in which she was a life beneficiary, and as co-trustee had the following powers (R. 15-16):

5. The Trustees shall have full power and authority to manage and control the property from time to time included in said trust estate, to sell at public or private sale, to exchange, to borrow, to pledge, and to invest and reinvest. It is expressly provided that the Trustees shall have the right and power to invest any moneys at any time or from



time to time in their hands in common stocks and preferred stocks of corporation organized under the laws of the Territory of Hawaii or elsewhere in the United States of America and shall not be limited by any statute or rule of law to the contrary. The Trustees shall treat all stock dividends and rights to subscribe as principal, and all cash dividends, whether regular or extraordinary, unless paid out of capital, as income. The Settlor expressly declares that the shares of corporation capital stock hereby assigned by him to the Trustees have proved satisfactory investments during a considerable period of time and that he does not wish them sold unless the Trustees in their discretion shall think it clearly advisable because of changing conditions or other special reasons. The Trustees shall not be held liable for any loss to the trust estate resulting from the retention of said stock by them.

Notwithstanding the settlor's declaration that he did not wish the securities sold, he did not close the door against their sale if deemed advisable. So, it may not be denied that Mrs. Sherman, as co-trustee, did have control over the income of the trust, and might have exercised that control so as to change the amount of income payable to her assignees, thus bringing her assignments within the rule of *Helvering v. Clifford*, 309 U. S. 331.

The taxpayer quotes (Br. 18-20) the dissenting opinion of Judge Arundell of the Tax Court in the case of *Farkas v. Commissioner*, 8 T. C. 1351, 1358, further in support of its contention that all the errors which the taxpayer attributes to the court below stem from a misconception of the rationale of the *Schaffner* case, *supra*. But we invite this Court to read the majority opinion in the *Farkas* case for an able rationalization



of the applicability of the rule of the *Horst* and *Schaffner* cases, to assignments of income by life beneficiaries of trusts comparable to that made by Mrs. Sherman in this case.

In the *Farkas* case the Tax Court very clearly points out why a person should be taxed upon the income which he assigns, when, as here, he retains the right to have that income at the termination of the assignment, which, as here, is for a period less than his life.

There is nothing in the courts' opinions in the case of *Hyman v. Nunan*, 143 F. 2d 425 (C. C. A. 2d), and the case of *Mahaffey v. Helvering*, 140 F. 2d 879 (C. C. A. 8th), cited on page 15 of the taxpayer's brief, contrary to the Collector's position here. Neither is the District Court's opinion in *Belknap v. Glenn*, 55 F. Supp. 631 (W. D. Ky.) (Br. 15), at variance with the Collector's position here. Similarly the opinion in *Huber v. Helvering*, 117 F. 2d 782 (App. D. C.) (Br. 15), supports the Collector's position here.

**B. The decision in the Blair case is not opposed to the Collector's position here**

The decision in the *Blair* case is not opposed to our position here. There, the life beneficiary of a trust irrevocably assigned a substantial portion of *his entire equitable life estate*. Accordingly, in that case the assignment of income was co-extensive with the assignor's entire estate in point of time as to the part thereof assigned. In the instant case this is not true. Here there was no transfer of any part of the assignor's life estate, but only of a specified number of dollars of income to which the assignor would be entitled if and when that amount of income might be earned by the trust. We think that the distinction mentioned is vital, and because of it, the decision in the *Blair* case is not opposed to our position here and is not controlling in the present case.

Such circumstances as those in the *Blair* case afforded basis for a holding that the assignor there did not retain enough of those prerequisites of ownership which the Supreme Court in *Helvering v. Clifford*, 309 U. S. 331, held to be determinative of tax liability. The situation here is materially different. Laura D. Sherman's equitable life estate in her husband's trust property was not assigned to anyone, in whole or in part; instead she merely carved out of that estate only a portion of the income, retaining the entire reversionary interest in the income so assigned upon the happening of designated events, all of which could occur in her lifetime. Thus her interest in the life estate remained intact after, as it was before, the assignment, wholly unaffected by it. There was no diminution of the interest of this beneficiary resulting from an assignment of a specified amount of the income which might be earned by the trust in a particular year and to which she was entitled.

If any of the assignees here received an interest in the Sherman trust which would entitle such assignee to enforce his or her rights as an owner of a beneficial interest in that trust as contradistinguished from merely the right to receive a certain number of dollars from the trustees if and when they were earned, the results would prove very perplexing indeed. For example, if for the year 1940 the taxpayer assigned an interest in the trust estate measured by \$3,000 of income in that year, then, if the assignees learned that the trustees contemplated changing the investments of the trust in such a way that the income thereof for the year 1940 would not amount to more than \$2,000, we submit that there is nothing the assignees could do to interfere with the trustees changing the investments of the trust. If the taxpayer's position is correct, the assignees would have the right to demand and require

that the trustees wholly disregard the effect upon trust income of the changed investments and make up the deficiency in income out of corpus. But it seems indisputable that the assignees did not acquire such an interest in the trust. It would seem therefore that the mere statement of such a proposition should refute the contentions of the taxpayer and demonstrate the fallacy of the taxpayer's argument that the assignees received an interest in the corpus of this trust by virtue of and as the result of the assignments in question. Thus there is only one other alternative right which inured to the assignees and that was only the right to enforce payment to them of the amounts of income provided in the assignments if and when that income was actually earned.

The instant case is more like the *Schaffner* case, *supra*, where the taxpayer carved out of her life estate a single year's income only. True, the assignees in the instant case had the right to receive income for a period which possibly might extend beyond a year, and in the case of the children, for as long as possibly ten years, but we submit that difference is merely one of degree, which, we believe, should not produce a difference in result taxwise. In any event, we believe the decision in the *Blair* case, *supra*, should be no more controlling here than it was in the *Clifford* and *Schaffner* cases. As we have hereinbefore pointed out, unlike the taxpayer in the *Blair* case, the taxpayer here did not assign to the assignees for her life all of her future interest in the income of the trust of which she was the sole life beneficiary. Instead, she merely assigned a specified number of dollars of that income for different periods not co-extensive with her life but which could have terminated before her death and, in the case of the children, did so terminate before her death. The *Blair* case limits the application of the doctrine of the

*Schaffner* and *Horst* cases only to the extent that a grant by the life beneficiary of her full interest in the income consists of a gift of the equitable interest in the corpus as well as of the income. As the Tax Court said in the case of *Farkas v. Commissioner*, 8 T. C. 1351, 1357:

The underlying reason why a gift of income unaccompanied by the gift of the property producing the income is ineffective to relieve the donor from the tax rests on the principle "that the power to dispose of income is the equivalent of ownership of it, and that the exercise of the power to procure its payment to another, whether to pay a debt or to make a gift, is within the reach of the statute, taxing income 'derived from any source whatever'".

The underlying reasoning in the cases relied upon by the Collector is that income is realized by the assignor because she, who owns or controls the source of the income, also controls the disposition of that which she could have received herself and diverts the payment from herself to others as a means of procuring a satisfaction of her wants. In other words the assignor has thus obtained the satisfaction of her desires where she collects and uses the income to procure those satisfactions or where she disposes of her right to collect it as a means of procuring them. In *Corliss v. Bowers*, 281 U. S. 376, 378, the Supreme Court said:

The income that is subject to a man's unfettered command and that he is free to enjoy at his own option may be taxed to him as his income, whether he sees fit to enjoy it or not.

Cf. *Helvering v. Eubank*, 311 U. S. 122. In the instant case each of the instruments making the assignments



contains a gift of a definite monthly sum to be paid (R. 43, 44)—

from the income to which the assignor now is or shall be entitled to receive as life beneficiary under the terms and provisions of that certain unrecorded trust deed dated December 26, 1935, executed by George Sherman as settlor \* \* \*.

Following the rationale of the District Court's opinion in *Bing v. Bowers*, 22 F. 2d 450 (S. D. N. Y.), affirmed without opinion, 26 F. 2d 1017 (C. C. A. 2d), no title to the trust estate or to any interest therein was created by the assignments, and the entire net income of the trust estate became gross income of the assignor notwithstanding the assignments of a part thereof to others.

**C. The taxing statutes fixes accountability for the tax upon the taxpayer because of her status as life beneficiary of the trust**

The internal revenue law itself, we submit, points to the correct solution of the instant problem. It deals explicitly with the liability of the estate or trust and reveals clearly where Congress intended to impose responsibility for the tax. Section 161(b) of the Internal Revenue Code (Appendix, *infra*) provides:

The tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary \* \* \*.

Section 162(b) of the Internal Revenue Code (Appendix, *infra*) provides:

There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries \* \* \* but the amount so allowed as a deduction shall be included



in computing the net income of the beneficiaries \* \* \*.

Since a tax statute is here involved, the import and reasonable construction thereof are controlling. The statute here is plainly worded. It imposes the liability for the tax on the beneficiary receiving trust income. No liability is placed upon her assignees, and, though they may have enforceable rights against the assignor in courts of equity, the taxing statute points unmistakably to the beneficiary as the one answerable for the tax. Thus, for tax purposes the taxpayer's status in the present proceeding as beneficiary of the trust dated December 26, 1935, is unalterably fixed. Even if equity may regard the assignment in this case as extinguishing the taxpayer's rights *in rem* as equitable owner of the trust *res* or her rights in *personam* against the trustee, the tax statute, nevertheless, fixes the accountability for the tax upon the taxpayer because of her status as beneficiary. So, even if it is assumed that the daughter-in-law and the children became beneficial owners of part of the income which the taxpayer received from the trust, it is still true that she, and not they, was the beneficiary of the trust, and that they had only a *derivative* interest. The very assignments in this case are bottomed on the fact that the income was the taxpayer's property, else there would have been nothing on which they could operate. Cf. *Poe v. Seaborn*, 282 U. S. 101.

It is, therefore, immaterial whether the law considers an equitable interest for life or for a term of years as present property, alienable like any other. Even though a beneficiary's interest is alienable, assignments of income are ineffective for tax purposes. It is clear from a reading of the assignments here involved that they dealt only with a right to receive income, and no

attempt was made to assign an equitable right, title or interest in the trust itself. The pertinent language of each assignment reads as follows (R. 43) :

\* \* \* the undersigned, Laura D. Sherman, hereinafter referred to as the assignor, does hereby assign, transfer and set over unto \* \* \* [name of donee], hereinafter referred to as the assignee, the sum of \* \* \* a month from the income to which the assignor now is or shall be entitled to receive as life beneficiary under the terms and provisions of that certain unrecorded trust deed dated December 26, 1935, \* \* \*.

Thus, in substance, the assignments are powers of attorney to receive the income to which the taxpayer "now is or shall be entitled to receive." When the assignees collect under these instruments, they do not collect their own income. By the terms of the instruments they are to collect the income due to the taxpayer.

#### CONCLUSION

The judgment of the District Court is correct and in accordance with the law and authorities. It should therefore be affirmed upon review of this Court.

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*Special Assistants to the  
Attorney General.*

RAY J. O'BRIEN,  
*United States Attorney.*

September, 1948.

## APPENDIX

## Internal Revenue Code:

## SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. In the case of Presidents of the United States and judges of courts of the United States taking office after June 6, 1932, the compensation received as such shall be included in gross income; and all Acts fixing the compensation of such Presidents and judges are hereby amended accordingly.

\* \* \*

(26 U. S. C. 1946 ed., Sec. 22.)

## SEC. 161. IMPOSITION OF TAX.

(a) *Application of Tax.*—The taxes imposed by this chapter upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

(4) Income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) *Computation and Payment.*—The tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary \* \* \*.

\* \* \*

(26 U. S. C. 1946 ed., Sec. 161.)

#### SEC. 162. NET INCOME.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

\* \* \*

(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall



not be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year;

\* \* \*

(26 U. S. C. 1946 ed., Sec. 162.)

Treasury Regulations 103, promulgated under the Internal Revenue Code:

SEC. 19.22(a)-1. *What Included in gross income.*

—Gross income includes in general compensation for personal and professional services, business income, profits from sales of and dealings in property, interest, rent, dividends, and gains, profits, and income derived from any source whatever, unless exempt from tax by law. \* \* \*

SEC. 19.161-1 [as amended by T. D. 5194, 1942-2 Cum. Bull. 53]. *Imposition of the tax.*—(a) *Scope.*

—Supplement E (sections 161 to 171, inclusive) prescribes that the taxes imposed upon individuals by chapter 1 shall be applicable to the income of estates or of any kind of property held in trust. The rate of tax, the statutory provisions respecting gross income, and, with certain exceptions, the *same* also to estates and trusts.

The several classes enumerated and described in the four paragraphs of section 161(a), and which are introduced by the word “including,” do not exclude others which also may come within the general purpose of that subsection.

The several classes enumerated and described in the four paragraphs of section 161(a), and which are introduced by the word “including,” do not exclude others which also may come within the general purpose of that subsection.

A guardian, whether of an infant or other person, is a fiduciary (see section 3797(a) (6)), and,

as such, is required to make and file the return for his ward and pay the tax, or the return may be made by the ward. (See section 19.51-1 and 19.142-2.) The estate of a ward is not a taxable entity, in that respect differing from the estate of a deceased person or of a trust.

The provisions of sections 161, 162, and 163 (relating to estates and trusts, fiduciaries, and beneficiaries) contemplate that the corpus of the trust, or the income therefrom, is, within the meaning of the Internal Revenue Code, no longer to be regarded as that of the grantor. If, by virtue of the nature and purpose of the trust, the corpus or income therefrom remains attributable to the grantor, these provisions do not apply. Thus the provisions of sections 166 and 167 deal with certain trusts which are excluded from the scope of sections 161, 162, and 163. Other trusts, not specified in sections 166 and 167, where in contemplation of law the corpus of the trust or the income therefrom is regarded as remaining in substance that of the grantor are likewise excluded from the scope of sections 161, 162, and 163. Some of such trusts are dealt with in sections 19.166-1 and 19.167-1. So-called alimony trusts to which section 22(k) or section 171 applies may be of a type to which the provisions of sections 161, 162, and 163 also apply, or of a type which is excluded from the provisions of sections 161, 162, and 163. Except to the extent that section 22(k) or section 171 governs the taxability of amounts paid, credited or to be distributed attributable to trust property, the treatment of such trusts under sections 161, 162, and 163 or under sections 166 and 167 is not affected by section 22(k) or section 171. See section 165 as to the exemption of employees' trusts.

(b) *Taxability of the income*.—The fiduciary is required to make and file the return and pay the tax on the net income of the estate or trust except as otherwise provided in sections 165, 166, and 167, and sections 19.166-1 and 19.167-1. In determining whether there is any net income subject to tax and the amount thereof, consideration is to be given to the additional deductions authorized in section 162.

SEC. 19.162-1 [as amended by T. D. 5196, 1942-2 Cum. Bull. 96, and T. D. 5215, 1943 Cum. Bull. 70]. *Income of estates and trusts*.—In ascertaining the tax liability of the estate of a deceased person or of a trust, there is deductible from the gross income, subject to exceptions, the same deductions which are allowed to individual taxpayers. See generally section 23, and the provisions thereof governing the right of deduction for depreciation and depletion in the case of property held in trust. Amounts allowable under section 812(b) as a deduction in computing the net estate of a decedent are not allowed as a deduction under section 23, except subsection (w), in computing the net income of the estate unless there is filed in duplicate with the return in which the item is claimed as a deduction a statement to the effect that the items have not been claimed or allowed as deductions from the gross estate of the decedent under section 812(b) and a waiver of any and all right to have such item allowed at any time as a deduction under section 812(b). For items not deductible, see section 24. Against the net income of the estate or trust there are allowable certain credits, for which see sections 25 and 163.

From the gross income of the estate or trust there are also deductible (either in lieu of, or in addition to, the deductions referred to in the preceding paragraph of this section) the following:

\* \* \*

(b) Any income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to a legatee, heir, or beneficiary, whether or not such income is actually distributed. For this purpose, it is provided in section 162(b), as amended by the Revenue Act of 1942, that "income which is to be distributed currently" includes income of the estate or trust which, within the taxable year, becomes payable to the legatee, heir, or beneficiary.

(c) Any income of the estate of a deceased person for its taxable year which is property paid or credited during such year to a legatee or heir, and any income either of such an estate or of a ~~deductions and credits allowed to individuals ap-~~ trust for its taxable year which is similarly paid or credited during that year to a legatee, heir, or beneficiary if there was vested in the fiduciary a discretion either to distribute or to accumulate such income.

\* \* \*

Any amount described in (b) and (c) of this section of the regulations as being deductible from the gross income of the estate or trust shall be included in computing the net income of the legatees, heirs, or beneficiaries, whether distributed to them or not.



No. 11909

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United States  
**CIRCUIT COURT OF APPEALS**  
*For The Ninth Circuit*

HAWAIIAN TRUST COMPANY, LIMITED,  
Executor of the Will of Laura D. Sherman,  
Deceased,  
Appellant,

vs.

AGNES M. KANNE,  
Executrix under the Will of Fred H. Kanne,  
Deceased,  
Appellee.

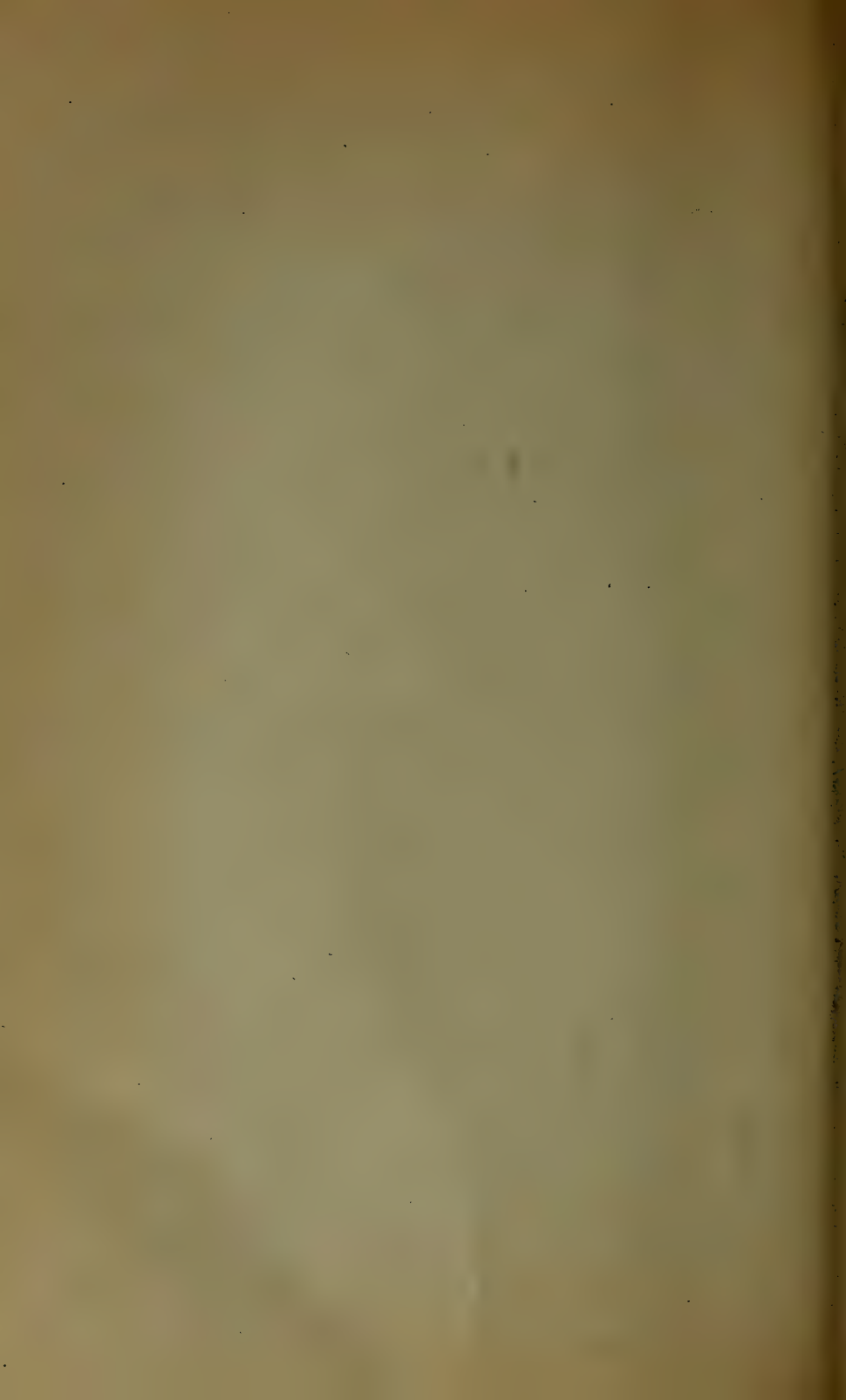
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REPLY BRIEF FOR HAWAIIAN TRUST COMPANY, LIMITED, EXECUTOR OF THE WILL OF LAURA D. SHERMAN, DECEASED

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*On Appeal from the District Court of the United States  
for the Territory of Hawaii*

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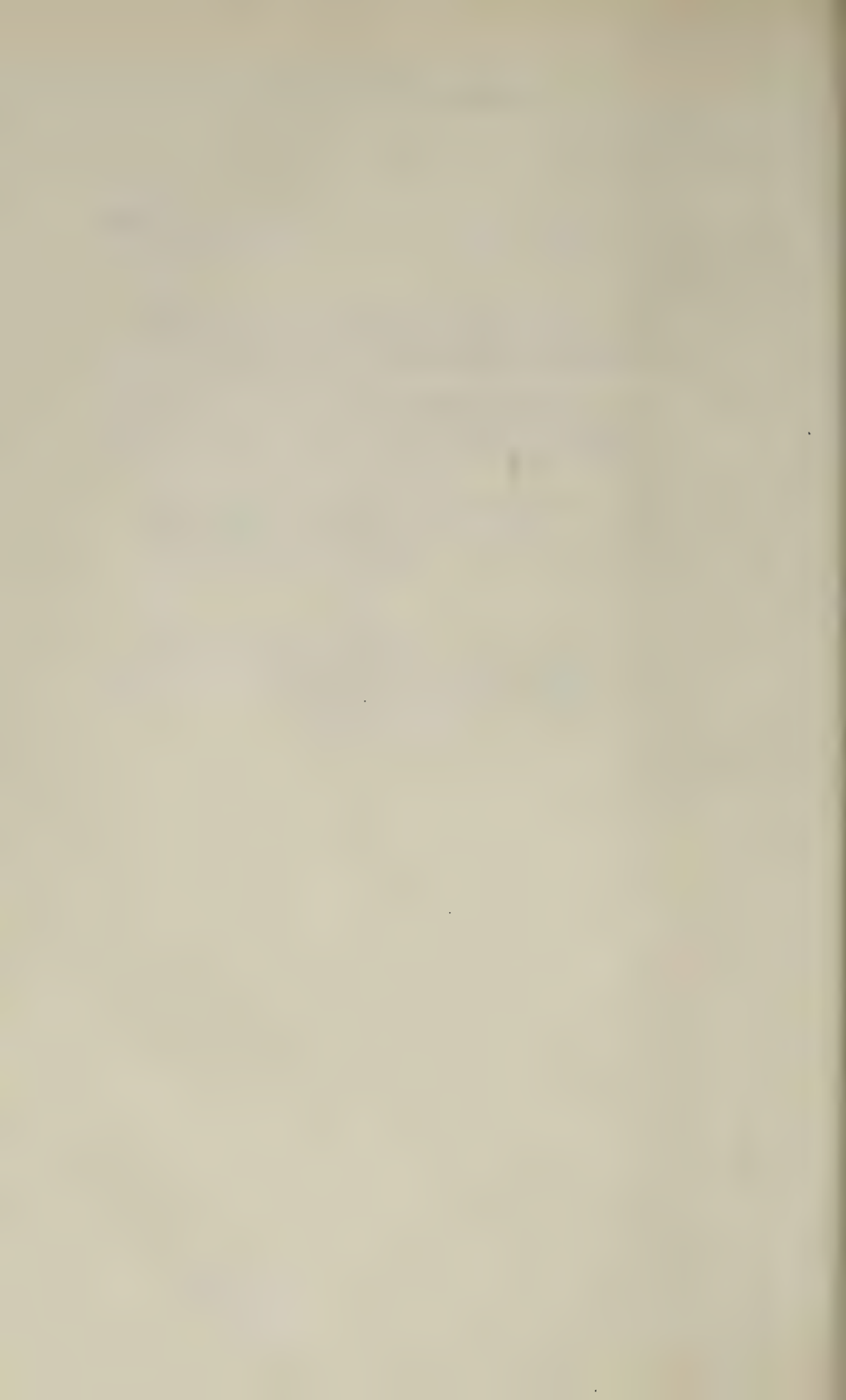




## SUBJECT INDEX

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	Pages
INTRODUCTION .....	1
ARGUMENT:	
1. THE ASSIGNEES ACQUIRED A PRO- PROPERTY INTEREST IN THE TRUST....	2
2. THE REVERSION RETAINED BY LAURA D. SHERMAN WAS NOT SUB- STANTIAL .....	4
3. THE PRESENT CASE IS NOT WITHIN THE FACTS, PURPOSE OR RULE OF <i>HELVERING V. CLIFFORD</i> , 309 U.S. 331, 60 S. Ct. 554 .....	5
4. SECTIONS 161(b) AND 162(b) OF THE INTERNAL REVENUE CODE DO NOT REQUIRE THE IMPOSITION OF TAX UPON THE ASSIGNOR .....	8
APPENDIX .....	10



# CITATIONS

---

## Pages

### CASES:

<i>Blair v. Commissioner</i> , 300 U.S. 5, 57 S. Ct. 330 .....	2, 3, 4, 9
<i>Harrison v. Schaffner</i> , 312 U.S. 579, 61 S. Ct. 759 .....	3
<i>Helvering v. Clifford</i> , 309 U.S. 331, 60 S. Ct. 554 .....	2, 3, 5, 6, 7, 8
<i>Helvering v. Horst</i> , 311 U.S. 112, 61 S. Ct. 144. .	3

### STATUTES:

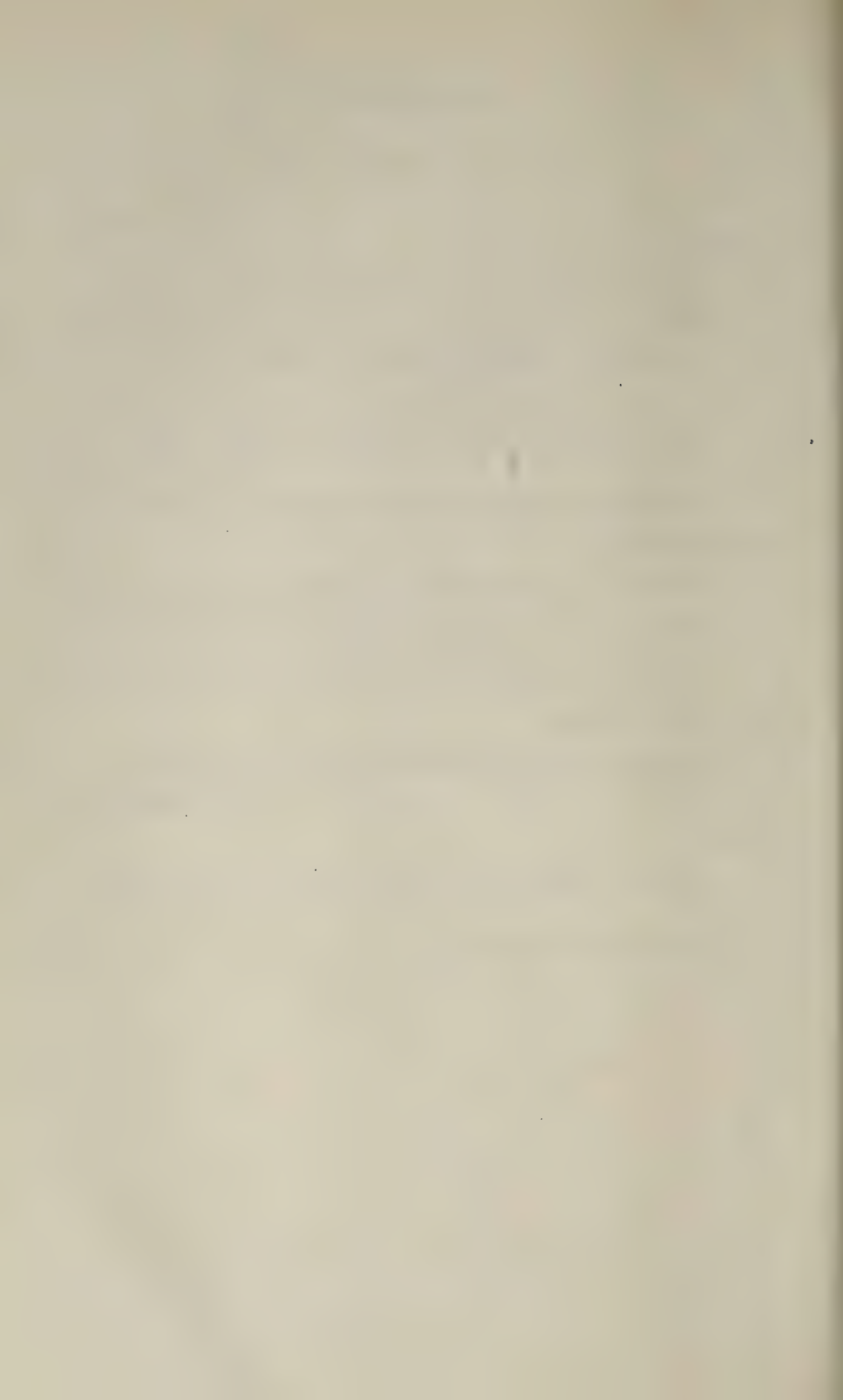
INTERNAL REVENUE CODE, Sec.22(a) . .	6, 8
INTERNAL REVENUE CODE, Sec.161(b) .	2, 8
INTERNAL REVENUE CODE, Sec. 162(b) .	2, 8

### REGULATIONS:

TREASURY REGULATIONS 111, Sec.29.22 (a)-21 .....	6, 7, 8, and Appendix
--	-----------------------

### TEXTS:

RESTATEMENT OF THE LAW OF TRUSTS .....	2, 3
SCOTT ON TRUSTS .....	2





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---

*On Appeal from the District Court of the United States  
for the Territory of Hawaii*

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INTRODUCTION

There are four principal contentions made in the brief for appellee:

1. That the assignments were of future income only, and the assignees acquired no interest in the principal of the trust.

2. That the assignor's reversionary interest constituted a substantial economic interest in the trust.

3. That the fact Laura D. Sherman was a co-trustee of the trust brings the case within the rule of *Helvering v. Clifford*, 309 U.S. 331, 60 S. Ct. 554.

4. That sections 161(b) and 162(b) of the Internal Revenue Code impose income tax on a named beneficiary of a trust but not upon her assignees.

We propose to answer these contentions and the arguments advanced in support of them in that order.

## ARGUMENT

### 1. THE ASSIGNEES ACQUIRED A PROPERTY INTEREST IN THE TRUST.

Appellee's contention that the assignments were <sup>OF</sup> future income only is unsupported by any authority. It overlooks the fact that the right to receive income from a trust is the genesis of a property right in the trust, because of the other rights concerning enforcement of the trust which necessarily go with that right to receive income. *Blair v. Commissioner* 300 U.S. 5, 57 S. Ct. 330, *Scott on Trusts* Sec. 130. Further, the right of an assignee of a beneficiary to enforce the trust is unquestioned. *Blair v. Commissioner supra*, *Restatement of the Law of Trusts* Sec. 200, Comment f.

The only support offered by appellee for the contention that income only was here assigned is the argument that technically less than the whole life interest

of Laura D. Sherman was transferred to her assignees. No authority is offered in support of this contention or argument. On the other hand, it is clear that a beneficiary may assign a *part* of his interest. *Restatement of the Law of Trusts* Sec. 132, Comment b. In *Harrison v. Schaffner*, 312 U.S. 579, 61 S. Ct. 759, relied on by the appellee, the Court recognized that an assignment by a life beneficiary of a trust of income for a period of a year was accompanied by a transfer of the property producing that income, saying at page 583 of 312 U.S.:

“Even though the gift of income be in form accomplished *by the temporary disposition of the donor's property which produces the income*, the donor retaining every other substantial interest in it, we have not allowed the form to obscure the reality.”

(Emphasis ours).

The *Blair* case and *Helvering v. Horst*, 311 U.S. 112, 61 S. Ct. 144, established that a transfer of income producing property is a necessary pre-requisite if the income therefrom is to be taxable to the assignee. The *Horst* case distinguished the *Blair* case on this ground. The *Schaffner* case accepts this but goes on to hold that that factor alone is not decisive in rendering assigned income taxable to the assignee and holds that the principles involved in *Helvering v. Clifford*, 309 U.S. 331, 60 S. Ct. 554, will be applied to determine whether a transfer of income producing property will result in the income therefrom being taxable to the transferor or the transferee.

Appellee also argues that the circumstance that the assignees would be unable to require an invasion of

corpus in the event the annual income of the trust fell below \$3,000 shows that the assignees had no interest in the "principal" of the trust. A similar assertion is made with respect to the provisions in Paragraph 13 of the trust (Tr. p. 18), which provides that the trust may not be amended to permit or authorize "the payment or application of the principal of the trust estate to or for the benefit of the Settlor's said wife". All this simply amounts to a discussion of the fact that Laura D. Sherman was an *income* beneficiary of the trust and that her assignees would acquire rights of the same nature. The fact that the trustees would not be entitled to take principal out of the trust and pay it to or expend it for the benefit of Laura D. Sherman or her assignees in no way establishes that Laura D. Sherman and her assignees did not have property interests in the trust. The beneficiary and his assignees in the *Blair* case also had no right to payments of principal, but the Court held that each had property interests in the trust. We submit that this latter portion of appellee's argument is not germane to the issues of this case.

## 2. THE REVERSION RETAINED BY LAURA D. SHERMAN WAS NOT SUBSTANTIAL.

The Appellee argues on pages 13 and 14 of his brief that if the interests assigned were substantial, it follows *a fortiori* that the reversion was substantial. Substantiality is a relative matter and this reasoning completely overlooks the disparity in the time and contingency factors affecting the relative substantiality of these interests. The interests assigned were all for terms in excess of ten years, or the reasonable equiva-



lent thereof, unless cut short by contingencies not as likely to occur as the contingency of the death of Laura D. Sherman prior to the termination of the assigned interests. Accordingly the interests assigned were far more substantial than the reversion of those same interests.

3. THE PRESENT CASE IS NOT WITHIN THE FACTS, PURPOSE OR RULE OF *HELVERING V. CLIFFORD*, 309 U.S. 331, 60 S. Ct. 554.

The appellee argues that Laura D. Sherman's powers as co-trustee bring the case within the rule of *Helvering v. Clifford*, *supra*. There is a similarity in the basic issue presented in the *Clifford* case and the present case but the facts of this case bear no resemblance to those found in *Clifford*. To state the facts of the *Clifford* case is an adequate refutation of appellee's argument. In *Clifford*, the taxpayer created a five year trust with himself as trustee and his wife as the exclusive beneficiary of income. All principal reverted to the taxpayer at the end of the five year term. The taxpayer as trustee had complete discretion as to the management and use of principal and the payment or accumulation of income. It was further conceded by the taxpayer that the "tax effects" of the creation of the trust were considered in connection with its creation. The Court stated that although none of these facts alone was decisive (the short duration of the trust, the intimate family relation, the tax avoidance aspects and the complete control of the grantor-trustee over the administration of the trust), taken collectively they were a sufficient basis for the finding that the husband was still the owner of the corpus for the purposes of section

22(a) of the Revenue Code. The Court was impressed ~~that~~ <sup>WITH</sup> the fact that the taxpayer's economic position was in this particular case substantially the same after the creation of the trust as before. Mrs. Sherman's situation could scarcely be similarly characterized as is pointed out in our opening brief at pages 15 to 17.

Appellee also argues that as co-trustee, Mrs. Sherman could have manipulated the investments so as to reduce the income payable under the assignments. Such a possibility is utterly fantastic but, assuming for the sake of argument that she might have done so, it would in no way have been an exercise of control which could have benefited her in any way or in any way have retained her economic position as it was prior to the execution of the assignments. This latter is the type of control contemplated in *Clifford* and in the Clifford Regulations. (Infra, Appendix). She was the income beneficiary of the trust and was not entitled to receive the principal thereof at any time and any control which she might have exercised as co-trustee is not the type of control nor could it be exercised for the purpose contemplated by the Court in the *Clifford* case. It should be pointed out, however, that under all the facts here, that (1) no such power of manipulation existed and (2) that there was not the faintest possibility of an attempt ever being made to exercise such power legally or illegally. During the years 1940 and 1941 income of the trust was in excess of nine and ten thousand dollars per year, respectively. (Tr. pp. 47-48). Because of the assignments, the assignees were entitled to \$3,000 annually of this income, Laura D. Sherman the balance. To affect the assignees at all a reduction of the income by more than two-thirds

would have been required. It is not within the bounds of reason to expect that this could have been accomplished without a breach of trust enjoined or redressable at the suit of the assignees. Accordingly, the practical power to make such manipulations never had any legal existence. Further, with respect to the possibility of an attempt to exercise such power, it should be remembered that it could not have been accomplished without the concurrence of the corporate co-trustee and would, of course, have resulted in complete and final loss to Laura D. Sherman of all income from the trust during such period. This is hardly the type of control which would have impressed the Court in the *Clifford* case, or any other court for that matter, as being a sufficient basis for a finding that this possible power resulted in the assignor remaining in substantially the same economic position after the assignment as he was in before.

A further answer to appellee's contention is supplied by the so-called Clifford Regulations (Regulations 111, Sec. 29.22(a)-21 *Infra*, Appendix). These regulations are not directly applicable here inasmuch as by their terms they apply to the taxability of trust income during the taxable years commencing January 1, 1946. They do, however, represent the views of the Commissioner of Internal Revenue as to the construction of section 22(a) of the Internal Revenue Code and his interpretation and extension of the *Clifford* rule, and he has announced a general policy of not asserting taxability of income in other taxable years, where such income would not be taxable under these regulations (Mim. 5968, Jan. 4, 1946). It so happens that by analogy to these regulations, the income assigned for



the two children is by precise provision of the regulations not taxable to the assignor, being either for their lives or for periods in excess of ten years, and without retention in the assignor of the powers of disposition or administration set forth in the regulations. The same is also true as to the assignment for the benefit of Anna Adams Nott. Every factor of the assignment, that is, the lack of retention of the powers of disposition or administration and termination of the interest upon the death of Anna Adams Nott, being specifically covered by the regulations. The only aspect of this transfer not covered by precise definition in the regulations is the possible termination on the contingency of her re-marriage. As to this, under the regulations, it would have to be determined whether the contingency was of "insubstantial character" in so far as the possibilities of Laura D. Sherman surviving the happening of that contingency was concerned. (Paragraph (c) of Sec. 29.22(a)-21. *Infra*, Appendix, p. 12). The contingency of re-marriage, being entirely outside the control of the assignor and one which might well never happen at all, can scarcely be classed as insubstantial. Yet despite all this and the further fact that the Clifford Regulations go far beyond anything established in the *Clifford* case, appellee has here contended that the assignments in this case come within the rule of the *Clifford* case.

#### 4. SECTIONS 161(b) AND 162(b) OF THE INTERNAL REVENUE CODE DO NOT REQUIRE THE IMPOSITION OF TAX UPON THE ASSIGNOR.

Appellee contends that sections 161(b) and 162(b) of the Internal Revenue Code tax the named benefici-



ary of the trust but not her assignees. Precisely the same argument was advanced by the government in the *Blair* case and it was finally and definitely rejected by the Supreme Court as follows:

“The Government points to the provisions of the revenue acts imposing upon the beneficiary of a trust the liability for the tax upon the income distributable to the beneficiary. But the term is merely descriptive of the one entitled to the beneficial interest. These provisions cannot be taken to preclude valid assignments of the beneficial interest, or to affect the duty of the trustee to distribute income to the owner of the beneficial interest, whether he was such initially or becomes such by valid assignment. The one who is to receive the income as the owner of the beneficial interest is to pay the tax.” (P. 12 of 300 U.S.).

Further comment by us seems unnecessary.

It is requested that the Judgment of Dismissal of the United States District Court for the Territory of Hawaii be reversed and set aside, and that court directed to enter judgment for plaintiff accordingly.

Respectfully submitted,

James M. Richmond,  
Attorney for Appellant,  
Hawaiian Trust Company, Limited,  
Executor of the Will of Laura  
D. Sherman, Deceased.

## APPENDIX

TREASURY REGULATIONS 111, SEC. 29.22(a)-21  
(Clifford Regulations)

Reg. 111, Sec. 29.22(a)-21. *Trust income taxable to the grantor as substantial owner thereof.*—(a) *Introduction.*—Income of a trust is taxable to the grantor under section 22(a) although not payable to the grantor himself and not to be applied in satisfaction of his legal obligations if he has retained a control of the trust so complete that he is still in practical effect the owner of its income. *Helvering v. Clifford*, 309 U.S. 331 (40-1 USTC ¶9265). In the absence of precise guides supplied by an appropriate regulation, the application of this principle to varying and diversified factual situations has led to considerable uncertainty and confusion. The provisions of this section accordingly resolve the present difficulties of application by defining and specifying those factors which demonstrate the retention by the grantor of such complete control of the trust that he is taxable on the income therefrom under section 22(a). Such factors are set forth in general in paragraph (b) and in detail in paragraphs (c), (d) and (e), below.

(b) *In general.*—In conformity with the principle stated in paragraph (a) above, the income of a trust is attributable to the grantor (except where such income is taxable to the grantor's spouse or former spouse under section 22(k) or 171) if—

(1) the corpus or the income therefrom will or may return after a relatively short term of years (see paragraph (c));

(2) the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition (other than certain excepted powers), whether by revocation, alteration or otherwise, exercisable by the grantor, or another person lacking a substantial adverse interest in such disposition, or both (see paragraph (d)) ; or

(3) the corpus or the income therefrom is subject to administrative control, exercisable primarily for the benefit of the grantor (see paragraph (e)).

(c) *Reversionary interest after a relatively short term.*—Income of a trust is taxable to the grantor where the grantor has a reversionary interest in the corpus or the income therefrom which will or may reasonably be expected to take effect in possession or enjoyment—

(1) within 10 years commencing with the date of the transfer, or

(2) within 15 years commencing with the date of the transfer if the income is or may be payable to a beneficiary other than a donee described in section 23(o) and if any one or more of the following powers of administration over the trust corpus or income are exercisable solely by the grantor, or spouse (living with the grantor, and not having a substantial adverse interest in the corpus or income of the trust), or both, whether or not exercisable as trustee: a power to vote or direct the voting of stock or other securities, a power to control the investment of the trust funds either by directing investments or reinvestments or by vetoing proposed investments or reinvestments, and a power to reacquire the trust corpus by substituting other property, whether or not of an equivalent value.

Where the grantor's reversionary interest is to take effect in possession or enjoyment by reason of some event other than the expiration of a specific term of years, the trust income is nevertheless attributable to him if such event is the practical equivalent of the expiration of a period less than 10 or 15 years, as the case may be. For example, a grantor is taxable on the income of a trust if the corpus is to return to him or his estate on the graduation from college or prior death of his son, who is 18 years of age at the date of the transfer in trust. Trust income is, however, not attributable to the grantor where such reversionary interest is to take effect in possession or enjoyment at the death of the person or persons to whom the income is payable.

In general, a reversionary interest may reasonably be expected to take effect in possession or enjoyment within 10 or 15 years, as the case may be, where the corpus or the income therefrom is to be reacquired if the grantor survives any stated contingency which is of an insubstantial character. Thus, the grantor is taxable where the trust income is to be paid to the grantor's wife for three years, and the corpus is then to be returned to the grantor if he survives such period, or to be paid to the grantor's wife if he is already deceased.

Any postponement of the date specified for the reacquisition of possession or enjoyment of the reversionary interest is considered a new transfer in trust commencing with the date on which the postponement is effected and terminating with the date prescribed by the postponement. But income for any period shall not be taxable to the grantor by reason of the preceding sentence if such income would not be taxable to him in the absence of such postponement.



*Example.* A places property in trust for the benefit of his son B. Upon the expiration of 12 years or the earlier death of B the property is to be paid over to A or his estate. Neither A nor his wife has any power of administration over the trust corpus or income. After the expiration of nine years A extends the term of the trust for an additional two years. A is considered to have made a new transfer in trust for a term of five years. He is not taxable on the income for the first three years of such term because he would not be taxable thereon if the term of the trust had not been extended. A is taxable, however, on the income for the remaining two years.

(d) *Power to determine or control beneficial enjoyment of income or corpus.*—Income of a trust is taxable to the grantor where, whatever the duration of the trust, the beneficial enjoyment of the corpus or the income therefrom is subject to a power of disposition (except as provided in section 167(c) and as hereafter provided in subparagraphs (1) to (4), inclusive), whether by revocation, alteration, or otherwise, exercisable (in any capacity and regardless of whether such exercise is subject to a precedent giving of notice or is limited to some future date) by the grantor, or any person not having a substantial adverse interest in the beneficial enjoyment of the corpus or income, whichever is subject to the power, or both. The grantor is not taxable, however, if the power, whether exercisable with respect to corpus or income, may only affect the beneficial enjoyment of the income for a period commencing 10 years from the date of the transfer (or 15 years where any power of administration specified in subsection (c) is exercisable solely by the grantor, or spouse living with the grantor, and not having a sub-

stantial adverse interest, or both, whether or not as trustee). For example, if a trust created on January 1, 1940 provides for the payment of income to the grantor's wife, and the grantor does not reserve any such administrative power but reserves the power to substitute other beneficiaries in lieu of his wife on or after January 1, 1950, the grantor is not taxable on the trust income for the period prior to January 1, 1950. But the income will be attributable to the grantor for the period beginning on such date unless the power is relinquished. If the beginning of such period is postponed, such postponement is considered a new transfer in trust commencing with the date on which the postponement is effected and terminating with the date prescribed by the postponement. But income for any period shall not be taxable to the grantor by reason of the preceding sentence if such income would not be taxable to him in the absence of such postponement. Where the income affected by the power is for a period beginning by reason of some event other than the expiration of a specific term of years, the grantor will be taxable if such event is the practical equivalent of the expiration of a period less than 10 or 15 years, as the case may be, in accordance with the criteria stated in paragraph (c).

The foregoing provisions of this paragraph shall not apply to any one or more of the following powers:

- (1) a power exercisable only by will, other than a power in the grantor to appoint the income of the trust where the income is accumulated for such disposition by the grantor, or may be so accumulated in the discretion of the grantor, or any person not having a substantial adverse interest in the disposition of such income, or both. For ex-

ample, if a trust provides that the income is to be accumulated during the grantor's life and that the grantor may appoint the accumulated income by will, the grantor is taxable on the trust income;

(2) a power to determine the beneficial enjoyment of the corpus or the income therefrom if such corpus or income, as the case may be, is irrevocably payable for the purposes and in the manner specified in section 23(o);

(3) If (i) the power is exercisable by a trustee or trustees, none of whom is the grantor, spouse living with the grantor, or a related or subordinate trustee of the type and under all the conditions referred to in subparagraph (4) (ii), and (ii) the exercise of the power is not subject to the approval or consent of any person other than such trustee or trustees, this paragraph shall not apply to a power—

(A) to distribute, apportion, or accumulate income to or for a beneficiary or beneficiaries, or to, for, or within a class of beneficiaries,

(B) to pay out corpus to or for a beneficiary or beneficiaries or to or for a class of beneficiaries (whether or not income beneficiaries).

The powers herein described include all the powers described in subparagraph (4), since the latter powers are more limited than those herein described.

(4) If the power—

(i) is exercisable by the grantor or spouse living with the grantor, or both, whether or not as trustee, or

(ii) is exercisable (A) solely by a trustee or trustees who include the father,

mother, issue, brother, sister, or employee of the grantor, or a subordinate employee of a corporation in which the grantor is an executive or in which the stockholdings of the grantor and the trust are significant from the viewpoint of voting control, and (B) in a manner which may affect the interests of beneficiaries which include the spouse or any child of the grantor (see subparagraph (3) for a power exercisable by a related or subordinate trustee of the class hereinabove described where the exercise of the power does not affect the interest of the spouse or a child of the grantor or where the power is exercisable only with the concurrence of an unrelated and non-subordinate trustee), or

(iii) is exercisable by any person or persons other than as trustee, or

(iv) is exercisable by any trustee or trustees, and the exercise of the power is subject to the approval or consent of any person or persons (other than such trustee or trustees), or of the grantor or spouse living with the grantor, or both, in the capacity of trustee,

this paragraph shall not apply—

(aa) to a power to pay out corpus to or for a beneficiary or beneficiaries or to or for a class of beneficiaries (whether or not income beneficiaries), provided that the power is limited by a reasonably definite external standard. Such standard must be set forth in the trust instrument and must consist of needs and circumstances of the beneficiaries;

(bb) if the power is not limited by a reasonably definite external standard, to a power to pay out corpus to or for any current income beneficiary, provided that any such



payment of corpus must be chargeable against the proportionate share of corpus held in trust for the payment of income to such beneficiary as if such corpus constitutes a separate trust;

(cc) to a power to distribute or apply income to or for any current income beneficiary or to accumulate such income for him, provided that any accumulated income must ultimately be payable to the beneficiary from whom distribution or application is withheld, to his estate, or to his appointees (or persons named as alternate takers in default of appointment) provided that such beneficiary possesses a power of appointment which does not exclude from the class of possible appointees any person other than the beneficiary, his estate, his creditors or the creditors of his estate; or, if payable upon the termination of the trust or in conjunction with a distribution of corpus which distribution is augmented by such accumulated income, is ultimately payable to the current income beneficiaries in shares which have been irrevocably specified in the trust instrument. Accumulated income shall be considered so payable although it is provided that if any beneficiary does not survive a date of distribution which may reasonably be expected to occur within the beneficiary's lifetime, the share of such deceased beneficiary is to be paid to such persons as the beneficiary may appoint, or is to be paid to one or more designated alternate takers (other than the grantor or the grantor's estate) if the share of such alternate taker or the shares of such alternate takers have been irrevocably specified in the trust instrument;

(dd) to a power, exercisable only during (1) the existence of a legal disability of any



current income beneficiary, or (2) the period in which any income beneficiary shall be under the age of twenty-one years, to distribute or apply income to or for such beneficiary or to accumulate and add such income to corpus;

(ee) in a case falling under subdivision (ii) hereof, to a power to distribute, apportion, or accumulate income to or for a beneficiary or beneficiaries, or to, for, or within a class of beneficiaries, whether or not the conditions in subdivision (cc) or (dd) are satisfied, provided that such power is limited by a reasonably definite external standard. For the requirements of such standard, see subdivision (aa) hereof.

A power does not fall within the powers described in subparagraphs (3) and (4) if the trustee is enabled to add to the class of beneficiaries designated to receive the income or corpus, except insofar as provision may be made for after-born or after-adopted children. A mere power to allocate receipts as between corpus and income, even though expressed in broad language, is not deemed a power over beneficial enjoyment with respect to income or corpus.

(e) *Administrative control.* — Income of a trust, whatever its duration, is taxable to the grantor where, under the terms of the trust or the circumstances attendant on its operation, administrative control is exercisable primarily for the benefit of the grantor rather than the beneficiaries of the trust. Administrative control is exercisable primarily for the benefit of the grantor where—

(1) a power exercisable by the grantor, or any person not having a substantial adverse interest in its exercise, or both, whether or not in the capacity of trustee, enables the grantor or any person to purchase, exchange or otherwise deal with

or dispose of the corpus or the income therefrom for less than an adequate and full consideration in money or money's worth; or

(2) a power exercisable by the grantor, or any person not having a substantial adverse interest in its exercise, or both, whether or not in the capacity of trustee, enables the grantor to borrow the corpus or income, directly or indirectly, without adequate interest in any case, or without adequate security except where a trustee (other than the grantor or spouse living with the grantor) is authorized under a general lending power to make loans without security to the grantor and other persons and corporations upon the same terms and conditions; or

(3) the grantor has directly or indirectly borrowed the corpus or income and has not completely repaid the loan, including any interest, before the beginning of the taxable year; or

(4) any one of the following powers of administration over the trust corpus or income is exercisable in a non-fiduciary capacity by the grantor, or any person not having a substantial adverse interest in its exercise, or both: a power to vote or direct the voting of stock or other securities, a power to control the investment of the trust funds either by directing investments or reinvestments or by vetoing proposed investments or reinvestments, and a power to reacquire the trust corpus by substituting other property of an equivalent value.

If a power is exercisable by a person as trustee, it is presumed that the power is exercisable in a fiduciary capacity primarily in the interests of the beneficiaries. Such presumption may be rebutted only by clear and convincing proof that the power is not exercisable primarily in the interests of the beneficiaries. If a power is not exercisable

by a person as trustee, the determination of whether such power is exercisable in a fiduciary or a nonfiduciary capacity depends on all the terms of the trust and the circumstances surrounding its creation and administration. For example, where the trust corpus consists of diversified stocks or securities of corporations the stock of which is not closely held and in which the holdings of the trust, either by themselves or in conjunction with the holdings of the grantor, are of no significance from the viewpoint of voting control, a power with respect to such stocks or securities held by a person who is not a trustee will be regarded as exercisable in a fiduciary capacity primarily in the interests of the beneficiaries. Where the trust corpus consists of stock or securities of a closely-held corporation, such a power may or may not, depending upon all the facts, be considered exercisable in a fiduciary capacity.

The mere fact that a power exercisable by the trustee is described in broad language does not indicate that the trustee is authorized to purchase, exchange, or otherwise deal with or dispose of the trust property or income for less than an adequate and full consideration in money or money's worth, or is authorized to lend the trust property or income to the grantor without adequate interest. On the other hand, such authority may be indicated by the actual administration of the trust.

(f) *Limitations of section.*—Despite the limitations of this section, the grantor of a trust directing the payment or application of the income therefrom in satisfaction of the grantor's legal obligations shall continue to be taxable on the income. The grantor may also be taxable on the income of a trust on the ground that such income is attributable to him in a capacity unrelated to dominion and control over the trust as such are de-

fined in subsections (c), (d) and (e) of this section. Thus, the provisions of this section do not affect the principles governing the taxability of future income to the assignor thereof whether or not the assignment is by means of a trust. Nor, for example, do the provisions of this section affect the applicability of section 22(a) to the creator of a family partnership. See further sections 166 and 167.

Section 22(a) shall be applied in the determination of the taxability of trust income for taxable years beginning prior to January 1, 1946 without reference to this section.





In The  
**United States Circuit Court of Appeals**  
**For the Ninth Circuit**

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JOSEPH CECIL MCKINNEY,  
*Appellant,*

VS.

UNITED STATES OF AMERICA,  
*Appellee.*

**APPELLEE'S ANSWERING BRIEF**

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FILED

JUN 24 1948

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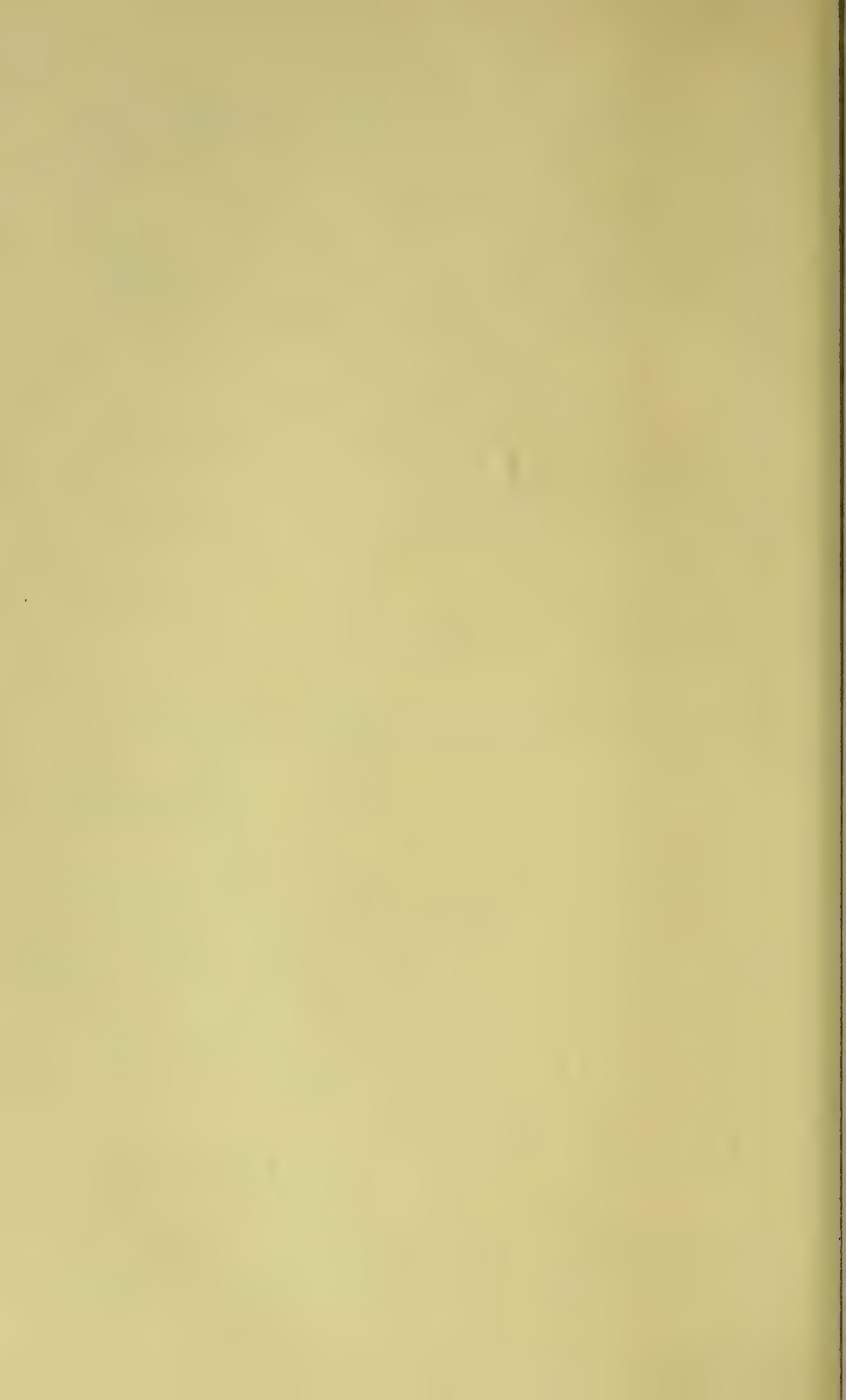
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# SUBJECT INDEX

	PAGE
Jurisdiction .....	1
Questions Presented for Review Upon Appeal.....	1
Argument:	
1 and 2	
The Information was fatally defective in that it omitted a material obligation	
Conviction based on information was improper.....	2
3	
The Verdict was not supported by the evidence.....	6
4, 5, 6	
Denial of appellant's request for witness Brannin	
Denial of examination of witness "Jim"	
Denial of examination of Prosecuting Attorney.....	8
7 and 8	
Prejudicial misconduct of Prosecuting Attorney	
Allowing references to gun to stand.....	9
9	
Admission of Mr. Eliason's answer that conversation with appellant took place in the "Los Angeles County Jail" .....	12
10	
Admission of irrelevant testimony on part of appellant..	13
11	
No Instruction was given by the Court defining "intent to defraud" .....	14
12	
The Court gave no instruction relative to finding intent to pass, publish, utter or sell, even though such in- tent was a necessary element in the proof of the crime, as charged .....	15
13	
The Court's Instruction No. 6 was prejudicial.....	15
Conclusion .....	16





## TABLE OF AUTHORITIES CITED

	PAGES
<i>United States v. Carll</i> , 105 U. S. 611; 26 L. Ed. 1135 .....	3
<i>United States v. Balint, et al</i> , 258 U. S. 251.....	3
<i>United States v. Behrman</i> , 258 U. S. 288.....	4
<i>United States v. Combs, et al</i> , 73 Fed. Supp. 813 .....	5
<i>United States v. Fawcett</i> , 115 F. (2d) 768 (8-9) .....	10
<i>Wege v. Safe Cabinet Co.</i> , 249 F. 697.....	12
<i>H. E. Winterton Gum Co. v. Autosales Gum and Chocolate Co.</i> , 211 F. 612.....	12
<i>Bachrack v. United States</i> , 75 F. (2d) 824.....	14
<i>Smith v. United States</i> , 74 F. (2d) 941.....	15
24 Corpus Juris Secundum 693.....	11
24 Corpus Juris Secundum 1065.....	13

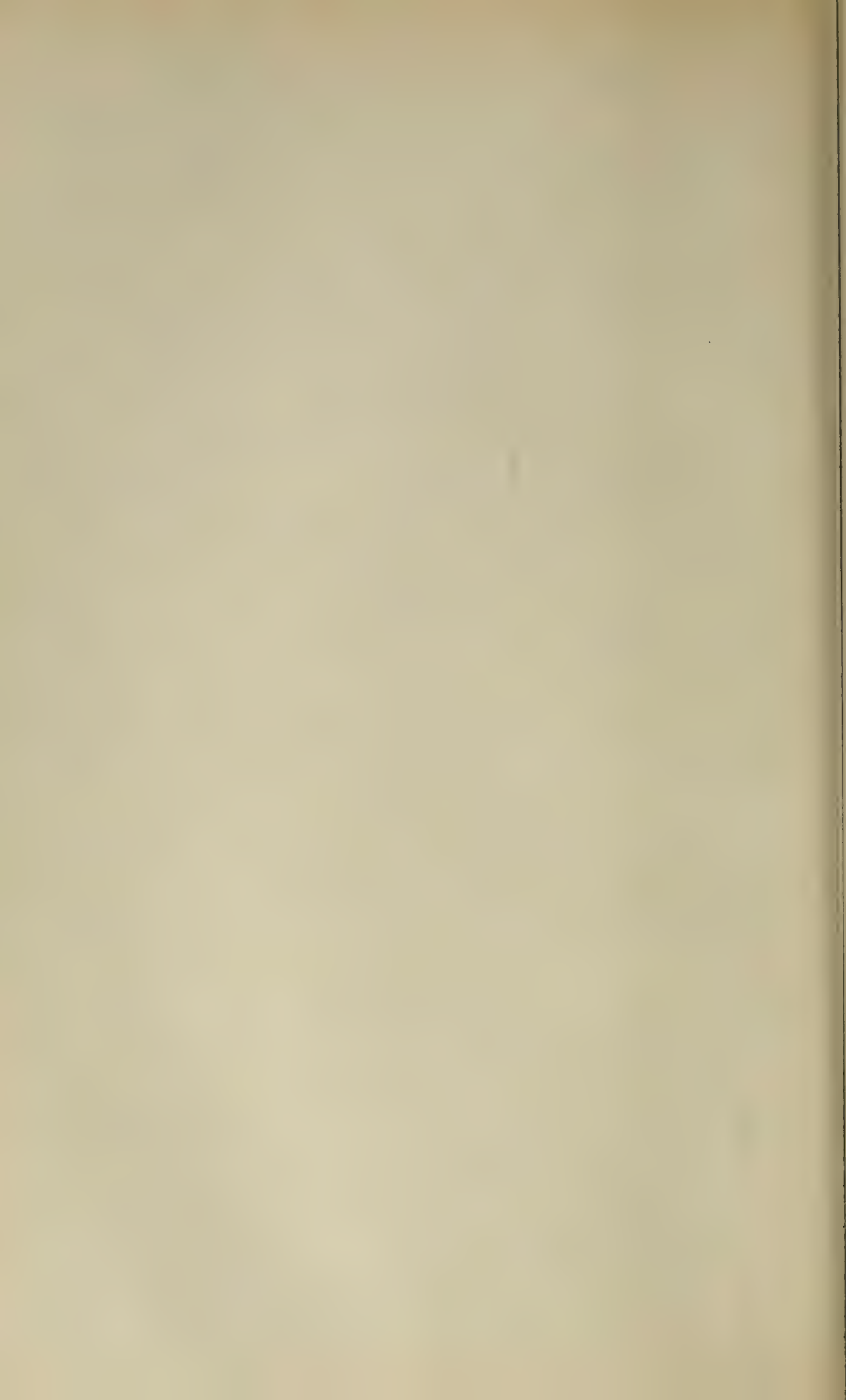
### Federal Constitution and Statutes

28 U. S. C. A. Sec. 225.....	1
18 U. S. C. A. Sec. 265.....	2, 9, 10, 14
18 U. S. C. A. Sec. 687.....	2, 6
18 U. S. C. A. Sec. 264.....	9, 10

### Rules of Court

#### Federal Rules of Criminal Procedure:

Rule 7 (b).....	2
Rule 7 (a).....	2
Rule 7 (c).....	3
Rule 34.....	6
Rule 35.....	6



No. 11,910

In The

**United States Circuit Court of Appeals  
For the Ninth Circuit**

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JOSEPH CECIL MCKINNEY,  
*Appellant,*

VS.

UNITED STATES OF AMERICA,  
*Appellee.*

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**APPELLEE'S ANSWERING BRIEF**

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**JURISDICTION**

The judgment of the United States District Court for the District of Nevada was entered on October 3, 1947 (T. R. 52-55) under which the defendant was committed to the custody of the Attorney General for five years on each of the two counts, said terms to run concurrently, and fined One Dollar (\$1.00) on each count.

From this judgment the defendant appeals for a review of the judgment under Sec. 225, U. S. C. A. Title 28.

**QUESTIONS PRESENTED FOR REVIEW  
UPON APPEAL**

The appellant has designated thirteen alleged errors under Specification of Errors, on pages 6-8 of Appellant's Opening Brief, but on page 8 thereof for the purpose of argument confines himself to two issues only. We shall address our reply to the alleged errors in the Specification of Errors.

## ARGUMENT

### 1 and 2

#### **The Information Was Fatally Defective In That It Omitted a Material Obligation.**

#### **Conviction Based on Information Was Improper.**

As the specified errors Nos. 1 and 2 are so closely related we shall consider them together. The Information (T. R. 3 and 4) consists of two counts charging violations of Sec. 265 T. 18, U. S. C. A. The Information was filed on July 30, 1947 and arraignment took place in the United States District Court for the District of Nevada on the same date (T. R. 48) after the appellant had in open Court signed a Waiver of Indictment (T. R. 49) under Rule 7(b) Federal Rules of Criminal Procedure, Sec. 687, T. 18, U. S. C. A. At the time of arraignment appellant was informed of his right to have counsel and the right to have his case presented to a Grand Jury. He was found to be fully cognizant of his rights and of the legal procedure involved, but declined to have an attorney and willingly signed the Waiver of Indictment before the Information was filed. Under Rule 7(a), Federal Rules of Criminal Procedure: "An offense which may be punished by imprisonment for a term exceeding one year or at hard labor shall be prosecuted by indictment or, if indictment is waived, it may be prosecuted by information." The offense for which appellant was prosecuted was punishable by a fine of not more than \$5000 and imprisonment of not more than fifteen years. Sec. 265 T. 18, U. S. C. A. The prosecution by information was in full compliance



with said Rule 7 of the Federal Rules of Criminal Procedure.

The second attack upon the information is that it did not state the appellant had knowledge of the altered condition of the obligations of the United States found in his possession. Both counts charge offenses in the language of the section violated and contain all the essential elements of the offenses with such definite clarity that the appellant was fully apprised of the charges he was called upon to meet and protected against future prosecution for the same offenses. Rule 7(c) Federal Rules Criminal Procedure requires: "The information shall be a plain, concise and definite written statement of the essential facts constituting the offense charged." The knowledge on the part of appellant that the Federal Reserve Notes in question were altered is one of proof upon the part of the government which was done in this case to the satisfaction of the jury.

The appellant relies upon the case of *United States v. Carll*, 105 U. S. 611; 26 L. Ed. 1135, (p. 9, Appellant's Opening Brief) that the information must allege he had knowledge of the alteration of the notes. That case was decided in 1882 and the statute under consideration was similar to the common law offense of uttering a forged or counterfeit bill. The offenses in the instant case are statutory and are governed by the well-established law that an indictment or information need not allege knowledge upon the part of the person charged where such offense is statutory and such knowledge is not made an element of the offense. In *United States v. Balint, et al*,

258 U. S. 251, Mr. Chief Justice Taft in the delivery of said opinion stated,

“While the general rule at common law was that the scienter was a necessary element in the indictment and proof of every crime, and this was followed in regard to statutory crimes even where the statutory definition did not in terms include it (*Reg. v. Sleep*, 8 Cox C. C. 472), there has been a modification of this view in respect to prosecutions under statutes the purpose of which would be obstructed by such a requirement. It is a question of legislative intent to be construed by the court. It has been objected that punishment of a person for an act in violation of law when ignorant of the facts making it so, is an absence of due process of law. But that objection is considered and overruled in *Shevlin-Carpenter Co. v. Minnesota*, 218 U. S. 57, 69, 70, in which it was held that in the prohibition or punishment of particular acts, the State may in the maintenance of a public policy provide ‘that he who shall do them shall do them at his peril and will not be heard to plead in defense good faith or ignorance.’ Many instances of this are to be found in regulatory measures in the exercise of what is called the police power where the emphasis of the statute is evidently upon achievement of some social betterment rather than the punishment of the crimes as in cases of mala in se. *Commonwealth v. Mixer*, 207 Mass. 141; *Commonwealth v. Smith*, 166 Mass. 370; *Commonwealth v. Hallett*, 103 Mass. 452; *People v. Kibler*, 106 N. Y. 321; *State v. Kinkead*, 57 Conn. 173; *McCutcheon v. People*, 69 Ill. 601; *State v. Thompson*, 74 Ia. 119; *United States v. Leathers*, 6 Sawy. 17; *United States v. Thompson*, 12 Fed. 245; *United States v. Mayfield*, 177 Fed. 765; *United States v. 36 Bottles of Gin*, 210 Fed. 271; *Feeley v. United States*, 236 Fed. 903; *Voves v. United States*, 249 Fed. 191.”

We further rely upon the law as set forth in *United*

*States v. Behrman*, 258 U. S. 288, paragraph 2, which states:

“It is enough to sustain an indictment that the offense be described with sufficient clearness to show a violation of law, and to enable the accused to know the nature and cause of the accusation and to plead the judgment, if one be rendered, in bar of further prosecution for the same offense. If the offense be a statutory one, and intent or knowledge is not made an element of it, the indictment need not charge such knowledge or intent. *United States v. Smith*, 2 Mason 143; *United States v. Miller*, Fed. Cas. 15,775; *United States v. Jacoby*, Fed. Cas. 15,462; *United States v. Ulrici*, Fed. Cas. 16,594, (Opinion by Miller, Circuit Justice); *United States v. Bayaud*, 16 Fed. 376,383-4; *United States v. Jackson*, 25 Fed. 548, 550; *United States v. Guthrie*, 171 Fed. 528, 531; *United States v. Balint*, ante, 250.”

An application of the law set forth in the two cases next above cited was made in the case of *United States v. Combs, et al*, 73 Fed. Supp. 813 by the United States District Court, Eastern District, Kentucky, on October 7, 1947, in a case parallel in legal principles to the one at bar in which that court overruled the defendant's motion to dismiss the indictment.

The trial court instructed the jury in Instruction No. 12, (T. R. 37) in an adequate and comprehensive manner upon the matter of knowledge and intent. A part of said instruction is as follows: “The jury must find beyond a reasonable doubt that the defendant kept such described altered security in his possession with knowledge of its character and with intent to defraud.”

The question of the sufficiency of the information is

raised for the first time on this appeal. The first step in laying a foundation for an appeal, if it is apparent that the information does not state a cause of action, is to challenge the same by a proper motion in the trial court. The Transcript of Record fails to show any motion before the judgment attacking the sufficiency of the information, on any ground, nor does it show any motion in arrest of judgment under Rule 34, Federal Rules of Criminal Procedure, 18 U. S. C. A. 687 et seq. or for a correction or reduction of sentence under Rule 35, Federal Rules of Criminal Procedure, 18 U. S. C. A. 687 et seq.

We believe the information was sufficient without alleging knowledge upon the part of the defendant that the Federal Reserve notes were altered; that prosecution by information was proper and that the conviction thereunder was justified and did not violate in any manner the rights of the defendant.

The "intent to defraud" is a comprehensive term and includes knowledge upon the part of the possessor of the character of the split notes which come under the terms of the statute involved as altered notes. We submit that it is difficult to conceive a situation where knowledge would not be part of a fraudulent intent.

### **The Verdict Was Not Supported by the Evidence.**

The trial record shows, and it is admitted by appellant, that he was found by the police officers to have in his possession one fifty dollar and one twenty dollar



Federal Reserve note, both of which were split in like manner, the front of each note being attached to a piece of celluloid and the back of each note also attached to celluloid and at the time of his arrest he was found to be in possession of one thousand new one dollar bills. The appellant claims he obtained the split bills and new bills from the home of a former friend and business associate, one George Harris, (Tr. T. 147, 154-156) and that he intended "setting a trap" (page 147) for Harris, "to keep him quiet" so that he could recover ten thousand dollars allegedly stolen by Harris from the appellant. On cross examination he stated he got those "thousand singles out of the bank" by exchange for hundred dollar bills (Tr. T. 152). Appellant testified (Tr. T. 147) that he got the split notes and the thousand new bills from George Harris's place the evening Mr. and Mrs. Haines drove him there. Mrs. Haines denied, on cross examination, that she saw him place any box in their car (Tr. T. 49). This took place on July 25, 1947 (Tr. T. 41). Appellant in his testimony refers to his ten thousand dollars whereas he claims eight thousand of this amount was entrusted to him by his landlady, Marian Jardine, (Tr. T. 141). The testimony of Mr. and Mrs. Haines and appellant shows that appellant took approximately sixteen hundred dollars from the Haines home in Los Angeles, California, on July 26, 1947. There was an understanding between Mrs. Haines and appellant that she would loan him this sum, but it was taken without her knowledge.

Appellant was arrested by the police in Reno, Nevada on July 28, 1947. The appellant was not charged with the

making of counterfeit bills nor with altering the two split bills. All the bills found in his possession were genuine obligations of the United States, including the split bills. He contends his possession of the split bills and the thousand new one dollar bills was for the purpose of forcing George Harris to return ten thousand dollars allegedly stolen from him. There was no proof offered by him of the truth of his having possessed such a sum of money so stolen by Harris. The record is silent of any request to have the landlady, Marian Jardine, appear in support of his contention although he testified she gave him eight thousand of the ten thousand dollars. We contend it would strain the credulity of any reasonable person to believe such a story and submit this to be a novel way to effect the collection of moneys unjustly taken from another. The evidence overwhelmingly supported the charge and justified the verdict.

4, 5, 6

**Denial of Appellant's Request for Witness Brannin.**

**Denial of Examination of Witness "Jim."**

**Denial of Examination of Prosecuting Attorney.**

Witness Miss Brannin was the public stenographer who typed the statement of appellant and, as stated on page 148 of the Transcript of Testimony, the statement was a repetition of his testimony. This statement was sent up on this appeal although it was only marked for identification.

Witness "Jim" was the jailor where appellant was

confined after his arrest and was only wanted as a witness to show that he took \$1.60 to pay for sending a telegram which was admitted in evidence. (Tr. T. 75).

The denial of appellant's right to examine the prosecuting attorney is specified as error. The record of this so-called denial appears on page 133, Transcript of Testimony and speaks for itself. The thousand one dollar bills were never in anyone's possession except the Reno Police and the Secret Service from the time of defendant's arrest until introduced in evidence as appears from the trial record.

The contention by appellant that the three denials of witnesses are errors is not grounded on reason. There was nothing that either could testify to that would assist the court or jury in properly deciding the issues involved. There was no denial of appellant's rights in either instance.

## 7 and 8

### **Prejudicial Misconduct of Prosecuting Attorney. Allowing References to Gun to Stand.**

Appellant's Specification of Errors Nos. 7 and 8 cover the prosecuting attorney's reference to a scheme on the part of defendant and the various references to the gun. The reference to the scheme on the part of the defendant was part of the government's case. In addition to the charge of violating Sec. 265, T. 18, U. S. C. A., he could have been charged with violation of Sec. 264, T. 18, U. S. C. A. for having in his possession a plate with intent to use the same in counterfeiting and the new bills which defendant had in his possession would be required for

such counterfeiting after bleaching in the collotype system of counterfeiting. The two offenses under Sections 265 and 264, T. 18, U. S. C. A., are so related that we contend it was entirely proper to show the scheme of the defendant in order to prove the intent to defraud and knowledge on his part. In *United States v. Fawcett*, 115 F. (2d) 768 (8-9), the court stated:

“It is a general rule of law that a distinct crime unconnected with that laid in the indictment cannot be given in evidence against a prisoner; *Shaffner v. Commonwealth*, 72 Pa. 60, 13 Am. Rep. 649; *Boyd v. United States*, 142 U. S. 450, 12 S.Ct. 292, 35 L.Ed. 1077. However, there are certain exceptions which allow the proof of other offenses in order to establish the intent or motive of the defendant if one or more of these elements must be proved in order that the guilt of the defendant may be established. The offense here charged is one in which intent and knowledge are requisite elements of proof, and accordingly the conduct of the defendant at or near the time charged in the indictment is admissible. The intention of a person charged with a crime can hardly ever be shown by direct evidence and for this reason it is permissible to introduce evidence of other acts of a similar nature; *Withaup v. United States*, 8 Cir., 127 F. 530; *Olson v. United States*, 8 Cir., 133 F. 849; *Colt v. United States*, 8 Cir., 190 F. 305; *Samuels v. United States*, 8 Cir., 232 F. 536, Ann. Cas. 1917A, 711. Here the act shown by the testimony complained of was connected with the offense charged in the indictment in that there was testimony by the government agent that the counterfeit ten dollar note given to Tierney was made from the same plates from which the counterfeit notes, G-1-G-8, were made. The intent as to other offenses was clearly interwoven in the offense charged and the evidence was admissible. *Parker v. United States*, 2 Cir., 203 F. 950.”



The references to the gun where allowed to stand were not improper. The defendant had the gun unlawfully in his possession and was arrested because of his attempt to exchange it for a higher caliber automatic revolver. His possession of a gun, the split notes and the new bills are not too unrelated as to be considered in arriving at the knowledge and intent to defraud required to be proven. The appellant in his own cross examination of Mr. Harding (Tr. T. 15-22) made repeated references to the gun and this should preclude him from raising objections to the conduct of his own case. The trial court's Instruction No. 18 (T. R. 41-42) and the court's ruling (Tr. T. 13) adequately protected the rights of the appellant.

It is a well-established principle that a party to a criminal proceeding cannot assume inconsistent positions in the trial and appellate courts. An appellant will not be permitted to allege errors in proceedings in the trial court in which he himself acquiesced or which were committed or invited by him or was the natural consequence of his own actions. Thus a party may be estopped to complain of a judgment for insufficiency of evidence where on the trial he supplied the deficiency by his own evidence or where he admitted the existence of facts which might otherwise have been proved. 24 Corpus Juris Secundum 693, paragraph 1842, with the many cases cited thereunder.

In the matter of the scheme above referred to on the part of the defendant concerning the collotype system of counterfeiting, the court's attention is called to the testi-



mony of Witness Walter Fisk (Tr. T. 88) describing this system, in which he states, on the last line of said page, that the plates (Exs. 1 and 2) are such plates as used in this system of counterfeiting, and on page 89, Transcript of Testimony, the same witness, in contradicting the contention of appellant, states that no photographic equipment is required in this process and only a small hand press is required or an old-fashioned washing wringer.

## 9

**Admission of Mr. Eliason's Answer That Conversation With Appellant Took Place in the "Los Angeles County Jail."**

There was no error, we contend, in the statement by Secret Service Agent Eliason that he interviewed the appellant in the Los Angeles County Jail. This was part of a proper foundation of the conversation the witness had with the appellant in establishing the time, place and circumstances under which the conversation took place. The appellant, in this Specification of Error, as in others, has failed to set forth any reason in support of the contention that this was error and that the rights of the defendant were prejudiced.

Where nothing more than the assignment of error is set out in the Brief it must be regarded as waived, *Wege v. Safe Cabinet Co.*, 249 F. 697; *H. E. Winterton Gum Co. v. Autosales Gum and Chocolate Co.*, 211 F. 612.

### **Admission of Irrelevant Testimony on Part of Appellant.**

This contention deals entirely with appellant's testimony, and in support of this alleged error argues that it was fantastic and prejudicial to him before the jury. We cannot disagree that it was fantastic, but it was his defense, and error would have been committed if he were denied the right to defend himself in his own manner. He was granted more freedom by the court and the prosecuting attorney in presenting his case, as the record shows, because he acted without counsel. It is well-established law that a defendant cannot complain of errors favorable to himself. 24 Corpus Juris Secundum 1065, paragraph 1932. We do not concede, however, that the greater latitude extended him was error.

We believe if defendant had been represented by counsel much of his confusing testimony and evidence would have been eliminated. This reference is to all assignments of error. Although no error has been assigned or specified that defendant was not represented by counsel during the trial or the various proceedings before or after trial except in the matter of this appeal, the record is replete with advice and efforts by the presiding United States District Court Judge to have counsel assigned (T. R. 48-51) (Tr. T. 1, 2). In addition to the foregoing the trial court did, on September 17, 1947, appoint Mr. Robert Adams, an able and experienced member of the Nevada Bar, to represent the defendant, but on September 19, 1947, permitted Mr. Adams to withdraw as counsel

because defendant desired to proceed without counsel. The Clerk of the United States District Court of Nevada has supplemented the Trial Record to cover the said appointment and withdrawal of counsel.

### **No Instruction Was Given by the Court Defining "Intent to Defraud."**

The "intent to defraud" is a comprehensive term as stated by the trial court. It is a term of such common knowledge to the average person required to serve on juries that further instruction was unnecessary. To require a specific definition of manner or effect of the defrauding would require also the name of the person, body politic, etc., to be named. In *Bachrack v. United States*, 75 F. (2d) 824, the court stated: "The statute (18 U. S. C. A. 265) uses the comprehensive term 'with intent to defraud' for the very purpose of making it immaterial whether the offender intended to defraud the government or some particular individual. One engaged in counterfeiting and kindred crimes may not, and probably does not usually, know who may be the victim of his fraudulent scheme; his real intention is that the forged instrument 'shall be accepted as genuine'."

We submit that the instructions generally, and particularly Instructions Nos. 9 and 12, adequately guided the jury in this connection.

**The Court Gave No Instruction Relative to Finding Intent to Pass, Publish, Utter or Sell, Even Though Such Intent Was a Necessary Element in the Proof of the Crime, as Charged.**

The information in each count is identical except the reference in count one refers to the \$50.00 note and count two refers to the \$20.00 note. Both charge that defendant "did unlawfully, with intent to defraud, and with intent to pass, publish, utter or sell, have or keep in his possession . . .". The intent to pass, publish, utter or sell is mere surplusage and, as it was unnecessary to sustain the violation, no instruction was necessary. In *Smith v. United States*, 74 F. (2d) 941, the Fifth Circuit Court of Appeals sustained a conviction based upon an indictment charging only "intent to defraud." The trial court's Instruction No. 12 (T. R. 37) correctly stated the law and there was no error committed by the omission of an instruction to pass, publish, utter or sell the said notes.

**The Court's Instruction No. 6 Was Prejudicial.**

The objection to the trial court's Instruction No. 6 (T. R. 34) is wholly without merit. Were this instruction standing alone it protects the rights of the accused in an adequate manner. This instruction considered with Instruction No. 5 (T. R. 33) in particular and all the instructions would warrant only the conclusion that the rights of the accused were fully protected in a manner

consistent with the conditions encountered in the trial by his appearing without counsel.

The fact that appellant refused assistance of counsel was a compelling reason for the trial court and the prosecuting attorney to exercise greater caution and consideration in their respective duties as the record shows.

### CONCLUSION

The appellant alleges thirteen errors. No objections were raised before, during or after the trial prior to this appeal. It is apparent that the appellant was not so disappointed with his conviction but rather with his sentence. Attention is called to his statement at the time of imposition of sentence (T. R. 53-4) when he stated, "Well, Judge, your Honor, I had a 100 per cent fair trial, there is nothing wrong with the trial at all. Of course, I disagree with the jury, but I had a 100 per cent trial."

We respectfully submit that there is no error, either assigned or argued by appellant or apparent in the record, to warrant a reversal of the judgment appealed from, and urge its affirmance.

DATED June 10, 1948.

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*United States Attorney*

BRUCE R. THOMPSON

*Assistant United States Attorney*

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*Assistant United States Attorney*

FEDERAL BUILDING

RENO, NEVADA

*Attorneys for Appellee*



No. 11911

IN THE  
**United States Court of Appeals**  
FOR THE NINTH CIRCUIT

---

CATHERINE O'CONNOR,

*Appellant,*

vs.

UNITED STATES OF AMERICA,

*Appellee.*

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**APPELLANT'S OPENING BRIEF**

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FILED

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# INDEX

## PAGE

### STATEMENT OF THE CASE

Statement of the Case .....	1
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### ARGUMENT

Argument .....	4
There was no offense proved against the Defendant and the Directed Verdict requested should have been given.....	4
Upon the Second Trial, the Prosecution refused to call Agent Tormey who was the Principal Investigator and Principal Witness in the First Trial and who prepared the accounts used by the Government in the First Trial. Defendant was required to call him as an adverse witness and the Court refused to permit the Defendant to examine him as an adverse witness.....	14
Although often demanded during the Trial, the Defendant was prevented from going into the basis of the Govern- ment's computations and accounts, refute the denuncia- tion or show the motive for its institution.....	18
A Bill of Particulars was timely requested. It was denied. The Defendant was surprised and the Items of Account in the Prosecution Account and Computation was refused inspection by the Defendant or to be put into evidence though repeatedly demanded .....	25
Much Admissible Testimony was excluded during the Trial	51
The Written Judgment does not conform to the Judgment pronounced by the Court.....	59
Numerous important instructions were requested by the De- fendant but not given by the Court.....	60
Conclusions .....	80

### TABLE OF AUTHORITIES CITED

Brown v. Brown, 170 Cal. 1, 147, p. 1168.....	65
Cole v. Commissioner, 9 Cir. 81 Fed. 2d, 485.....	72
Cooper v. U.S., 6 Cir. 9 Fed. 2d, 216.....	63

## ii.

	PAGE
Foster v. U.S., 253 Fed. 481 .....	43
Hargrove v. U.S., 67 Fed. 2d, 820.....	61, 62, 69
Herencia v. Guzman, 219 U.S. 44, 31 S.Ct. 135, 55 L.Ed. 81....	15
Hilpert v. Commissioner, 5 Cir. 151 Fed. 2d, 929.....	60
Hill v. U.S., 298 U.S. 460, 56 S.Ct. 760, 80 L.Ed. 1283.....	60
Kirby v. U.S., 174 U.S. 47, 19 S.Ct. 574, 43 L.Ed. 890.....	50
Loraine v. Loraine, 8 Cal. App. 2d, 687, 48 P. 2d. 48.....	65
Maxfield v. U.S., 152 Fed. 2d, 593.....	45
McDermott v. Commissioner, 150 Fed. 2d, 585.....	68
Noble v. U.S., 3 Cir. 284 Fed. 253.....	63
Lawrence Oliver v. Commissioner, 4 Tax Court 684.....	66
Paschen v. U.S., 70 Fed. 2d, 491.....	63
People v. Armentrout, 118 Cal. App. 761, 1 P. 2d, 556.....	63
Perez v. U.S., 10 Fed. 2d, 352 .....	49
Periera v. Periera, 156 Cal. 1, 103 P. 488.....	66
Roches v. Blair, 9 Cir. 32 Fed. 2d, 22.....	66
Rucker v. Blair, 9 Cir. 32 Fed. 2d, 222.....	7
Scotland County v. Hill, 112 U.S. 183, 5 S.Ct. 93, 28 L.Ed. 692 .....	15
Shaw v. U.S., 131 Fed. 3d 2d, 476.....	50
Singer v. U.S., 58 Fed. 2d, 74.....	43
Spies v. U.S., 317 U.S. 492, 87 L.Ed. 418.....	63
Stockton Sav. & Loan Bank v. Massanet, 18 Cal. 2d, 200, 114 P. 2d 592 .....	61
Suburban Fruit Lands Co. v. Soderman, 9 Cir. 36 Fed. 2d, 934 .....	15
U. S. v. Allied Chem. & Dye Corp. (DC-NY) 42 Fed. Supp. 425 .....	43, 49

### **iii.**

	<b>PAGE</b>
U. S. v. Empire State Paper Co. (DC-NY) 8 Fed. Supp. 220 .....	39, 41
U. S. v. Murdock, 290 U.S. 389, 54 S.Ct. 223, L.Ed. 381.....	69
U. S. v. Skidmore, 123 Fed. 2d, 604 .....	50
Washburn v. Commissioner, 5 Tax Court No. 162.....	68

### **STATUTES AND TEXTBOOKS**

California Civil Code, Section 172.....	65
3 CCH Federal Tax Reporting Service, 609, Sec. 120 et seq....	59
31 Corpus Juris, Page 750, Sec. 308.....	49
Current Tax Payment Act of 1943.....	73
28 USCA 638 .....	61





**No. 11911**

IN THE

**United States Court of Appeals**

FOR THE NINTH CIRCUIT

---

CATHERINE O'CONNOR,

*Appellant.*

vs.

UNITED STATES OF AMERICA,

*Appellee.*

---

**APPELLANT'S OPENING BRIEF**

---

**STATEMENT**

This is an appeal from the District Court's judgment of conviction of the defendant, Catherine O'Connor, upon an indictment under Sec. 145b of the Internal Revenue Code, in three counts, 1942, 1943 and 1944. A timely motion for a bill of particulars was made, upon a showing by affidavit. It was denied. Defendant plead not guilty to all three counts. A jury trial was had and the jury disagreed on all three counts. A second jury trial was had, and the jury convicted on the first count (1942) and disagreed on the other two. The Court

pronounced judgment of 6 months imprisonment and \$5000 fine, and made a different written judgment imposing imprisonment in default of payment of the fine.

The government called agent-investigator Krause who testified to the alleged income of defendant, putting into evidence the final totals by Exhibits 28, 29, and 30. Although demanded to be inspected by the defense, to be put into evidence, or to determine the items making up the sums testified to, all were denied; and defense never did have an opportunity to inspect the "work sheets" from which the witness testified, or to put them in evidence, or to learn the items or computations making up the totals testified to by Krause.

In the first trial, the principal investigator Agent Tormey testified as the principal witness to a different account and computations of income (materially different in most items, and smaller business receipts but larger net income). He was not called by the prosecution in the second trial, and it was necessary for the defense to call him as an adverse witness. The court did not permit impeachment, nor to go into the investigation nor motives of Tormey. It was learned that the same basic data was used in each government computation, with much different results; and that the accounts involved investigation of unknown third persons, and was not confined to the records in evidence.

The defendant was surprised, misled, and suf-

ferred prejudice by the failure to obtain the bill of particulars, or to discover the items making up the income, deductions, etc.

There are numerous errors assigned, and set forth in a separate writing filed in this cause. The questions, objections, and rulings specified as error; the instructions requested and not given, and the erroneous instructions given; and the portions of the record showing matters specified as error are set forth in the supplement of this brief.

Under the year of 1942 of which the defendant stands convicted the indictment charged "Gross Income" and under that "Net profit from bar \$2,785.50". The Krause figures, Exhibit 28, gives the comparable item of "corrected business income" as \$172.13. The Tormey first trial figures give the comparable item as \$1267.18.

The accused was a person of little education or experience in business. She acquired a half interest in the small bar on Valencia St., San Francisco, for \$1,000 in 1940. She married Jost in March, 1942. Upon the credit and savings of the community, she acquired the other half interest of the bar in July, 1942, for \$1650. She theretofore relied upon her partner for tax returns. Knowing her inadequacy, she employed an accountant of 30 years experience, provided him with records he requested, and she and her husband made the return prepared by the accountant. She was divorced from her husband in 1943 by an interlocutory decree silent as to property matter and by a final

decree in 1944 also silent on property. Because she alleged in her divorce complaint, upon which a default was taken, that she had no community property in July, 1943, the Court excluded all matters of community property or community property income during marriage. The divorced husband testified for the government. So did the accountant.

### ARGUMENT

**There was no offense proved against the Defendant and the Directed Verdict requested should have been given.**

The indictment charged the defendant in the first count (1942):

#### *Gross Income*

Net Profit from bar .....	\$2,785.92
Salaries .....	1,380.00
Rental income .....	303.00
Partnership income .....	2,116.05
	<hr/>
	\$6,584.97

#### Deductions:

Contributions .....	\$152.50
Interest paid .....	73.00
	<hr/>
	225.50

Net income.....\$6,359.47

The principal difference was *income from bar* (July 42 to end of year). Let us compare these differences with the evidence.

Exhibit 28 (Krause computations) Corrected bus. inc.....	\$ 172.13
Tormey's computations, corrected business income	
(Trans. 577) .....	1,267.18
Sum charged in the indictment.....	2,785.92



That the defendant's accountant, Bosserman, computed a different net income from bar<sup>1</sup> and defendant

<sup>1</sup>Actually the government witness Bosserman who computed and drew the original return, shows a loss, for the operations of the bar by the defendant from July 16, 1942, to Dec. 31, 1942. The partnership return does not reflect many deductions as loss from theft which was considerable as shown by the defendant's testimony nor does it contain usual items of business deductions as depreciation, etc. The government offered no evidence as to the partnership income, except the partnership return which we can assume understated deductions as Bosserman did in subsequent returns:

1942 Deductions (Bosserman computations in return) ..	\$11,082.81
1942 Deductions: Krause allowed in Pros. comp.	
(Tr. 425) .....	15,216.34

Deductions understated according to prosecution figures .....	\$ 4,123.53
1943 Deductions (Bosserman computations in return) ..	\$22,493.40
1943 Deductions—Krause allowed in Pros. comp.	
(Tr. 426) .....	28,676.53

Deductions understated according to pros. figures.....	\$ 6,183.13
1944 Deductions (Bosserman computations in return) ..	\$25,763.40
1944 Deductions—Krause allowed in pros. comp.	
(Tr. 426) .....	41,098.14

Deductions understated according to pros. figures.....	\$15,334.74
--	-------------

In fact Bosserman even omitted to deduct his own fee paid to himself by the defendant, as an allowable deduction, which is clearly an allowable deduction. Tr. 272.

A proof of the partnership income, we can infer, follows the same general pattern. The duty to prove the actual amount of income is an element which the prosecution, not the defendant bears.

and her husband, Jost, relied upon it and signed the return is not denounced as an offense by Congress.

Furthermore, the tax on the \$172.13 income shown by Exhibit 28 is a negligible sum.

Furthermore, there is a material variance seen in the allegations and the proof, for the allegations of the indictment for the principal item in dispute is net profit from bar charged at \$2,785.92 and the proof by Krause, Ex. 28, is \$172.13, a very substantial difference.

The indictment (second count) charges for 1943:

*Gross Income*

Net profits from bar.....	\$21,684.25
Rental income .....	324.66
	<hr/>
	\$22,008.91

Deductions:

Contributions .....	\$255.00
Taxes .....	155.00
	<hr/>
	410.00

Net income.....\$21,582.91

Evidence shows:

Tormey computations used at first trial by pros.

corrected business receipts (Tr. 571).....\$44,187.65

Krause computations used at second trial by pros.

corrected business receipts (Ex. 29)..... 46,506.45

Tormey computations, Other Income (Tr. 575)..... 324.66

Krause (second trial), Other Income (rents, Ex. 29)

LOSS .....

Tormey computations, Business Deductions (Tr. 574)..... 24,630.31

Krause computations, Business Deductions (Ex. 29).... 28,676.53

Bosserman computations, relied upon by defendant in

making 1943 return (Tr. 426), Business Deduction 22,493.40

These figures show that the defendant's accountant for the returns, and relied upon by the defend-

ant, computed business deductions far less than either of the government's computations. This would show no conscious effort to defeat or defraud the government.

Let us use the Government's figures most favorable to the defendant—1943:

Corrected Business receipts (Tormey, first trial).....	\$44,787.65
Business deductions (Krause, second trial).....	28,676.53
<hr/>	
Net profits from bar, using above government figures....	\$16,111.02
Other income (Krause, second trial figures) LOSS.....	28.60
<hr/>	
Net Income.....	\$16,082.42
Deductions alleged in indictment.....	410.00
<hr/>	
	\$15,672.42

The defendant was married to Jost in March, 1942, and lived with her husband in California until the separation in July, 1943, (government's testimony, Tr. 162) and the interlocutory decree in July, 1943, was silent as to community property, and the marriage was not dissolved until the final decree of divorce in 1944.

The presumption is that mixed property is wholly community.

*Rucker v. Blair*, 9 Cir. 32 F2d. 222.

And community property continues until the final decree of divorce dissolves the marriage and the community.

That on the date of filing of the divorce complaint, the community property up to that time had been spent (Tr. 761-2) does not effect this rule, and com-

munity property thereafter acquired continues until the final decree of divorce.

Thus half of the figure of \$15,672.42 shown above, from the government's various figures, is less than \$8,289.28 taxable income computed by Bosserman and relied upon by the defendant in her 1943 return and upon which she duly paid taxes.

The indictment, third count (1944), charged:

*Gross Income*

Net income from bar .....	\$24,579.05
Rental income .....	451.83
	<hr/>
	\$25,030.88
Deductions—Standard .....	500.00
	<hr/>
Net income.....	\$24,530.88

Evidence shows:

Corrected Business Income—(Krause, Ex. 30).....	\$54,004.30
Corrected Business Income—(Tormey, Tr. 569).....	50,342.45
Business Deductions—(Krause, Ex. 30).....	41,098.14
Business Deductions—(Tormey, Tr. 568) .....	23,052.30
Business Deductions—Bosserman in 1944 returns.....	25,763.40
Other income (rents—Krause, Ex. 30)—LOSS .....	1,295.74

Suppose we take the Government's computations most favorable to the defendant—1944:

Corrected Business Income (Tormey, Tr. 569).....	\$50,342.45
Business deductions (Krause, Ex. 30).....	41,098.14
	<hr/>
Income from bar on above.....	\$ 9,244.31
Other income (Krause, Ex. 30)—LOSS.....	1,295.74
	<hr/>
	\$ 7,448.57
Standard deduction .....	500.00
	<hr/>
	\$ 7,448.57

The community was not dissolved by divorce until



middle of 1944, and at that time the parties became tenants in common of the community property. Thus using a rough rule of thumb that one-half of these Government figure income of \$7,448.57 was earned before the community was dissolved, and half afterwards; thus one-fourth roughly would be chargeable to Jost and three-quarters would be reportable by the wife, and this figure would approximate the \$5,591.98 computed by Bosserman, entered by him on the 1944 return and relied upon by the defendant and upon which she paid her tax.

B.

There is a total lack of *willful intent* shown by the prosecution's own case and evidence. Mrs. O'Connor employed prosecution witness Bosserman as an accountant to prepare her returns, starting for the taxable year 1942. She provided him with her records. She did not instruct him to omit any part (Tr. 265). She filed the returns he prepared without change and without question (Tr. 236-7).

There was conflict in the evidence as to the defendant providing Bosserman with the bank statements and checks. However, Bosserman testified he would not have used the bank statements and cancelled checks and bills if she had brought them to him, in his work in preparation of the returns (Tr. 235). He knew she had a bank account and checking account (Tr. 268). He knew from his accounting work that other taverns and bars had income from music machines, pin ball and claw machines (Tr.



233). He was in the defendant's place of business several times (Tr. 232). and must have seen the obvious machines—a disclosure more vivid and positive than any verbal information from the defendant.

Certainly a person disclosing the existence of this income, the existence of the bank and checking account to a public accountant of 30 years' experience and licensed to practice before the Treasury in tax matters, has done all she can. The professional man judges what data and information he must have to perform the skilled services of a return, and the nature and extent of his services necessary to perform his employment. The defendant cannot tell him his business, but must rely upon his judgment. She did. She relied upon his skill and judgment. She submitted the returns he prepared and told her and her husband to sign, and they did. That two prosecution witnesses, agents in the Intelligent Unit, may have used these same records to arrive at two different and separate results is not criminal nor proof of a crime.

Aside from the prosecution witnesses' testimony, which included the work sheet of Mr. Bosserman showing checks as items from which it must be conclusive proof he had the checks before him to make that work sheet for the return he drafted; and aside from the letter of Mr. Bosserman showing that he knew the defendant had no knowledge of income tax matters and relied upon him, which was refused admission in evidence; the defense evidence shows that the entire records and memorandum of the de-

fendant was provided Bosserman for each return, before he prepared it. The defense evidence also shows that the defendant had never before prepared a return, but had relied upon her partner. The first time was 1942, when she and her husband had the responsibility of filing returns alone, and she realizing her lack of knowledge, hired a public accountant who held himself out as skilled and with years of experience, provided him with all the data and records he asked, and relied upon his judgment and skill.

C.

Mr. Barlow, a certified public accountant, a partner in a firm of certified public accountants in San Francisco, and a man skilled in income tax accounting work was called as an expert by the defense. He testified that on the basis of Government's Exhibit 28, etc., that there was *no* tax for 1942 (Tr. 532-5). Obviously, a party cannot be guilty of attempting to defraud the government of an income tax for a period in which there was no income tax.

Mr. Barlow was asked the same hypothetical question the prosecution expert was asked, using the Government's figures and evidence, for 1943, and upon which the Government contends it can prove a tax for the year 1943 by the answer of its expert. Mr. Barlow testified that it would be impossible to compute the 1943 tax from those figures and facts without making an assumption of fact (which assumption the trial judge ruled was assuming a fact not in evidence)—and which assumption would in-

volve a fact not in evidence at any part of the proceedings (Tr. 539-544). Obviously, there was no showing of any tax imposed on the defendant for the year 1943 and it was improper for the court to submit the second count (1943) to the jury, and refuse the directed verdict submitted for the second count. The jury disagreed for a second time on this **count**, as it did on the third count.

#### D.

As to the second and third counts in the indictment, there was no evidence offered, and no contention of any evidence that the defendant did anything within the Spies Case as an act amounting to a felony. That the Government agents might compute a different series of figures from the defendant's books and records, than the prosecution witness Bosserman did in his work and preparation of the returns in his professional employment by the defendant, is not fraud or even negligence, unless it was negligence in employing an accountant whose ultimate computations differed from the prosecution witnesses' computations. We might point out that Bosserman's computations did not vary or differ as greatly as the Government's indictment, the Government's figures in the first trial by Agent Tormey or the Government's figures in the second trial by Agent Krause differed, each from the other.

#### E.

All of the acts of the signing of the returns, in-

cluding the keeping of the books were done by the defendant in the presence of her husband.

It is a long established, basic concept of our jurisprudence, that acts done by a wife in the presence of her husband are presumed to be done at his compulsion.

Living in the same building is within the presence of the husband, raising the presumption that must be overcome by positive testimony of the prosecution. The evidence of the prosecution included prosecution witness Jost, the husband later divorced, and the prosecution's witness proved the facts raising the presumption (Tr. 162, 172, 176). See also defendant's testimony, Tr. 692, 698-9, 700, 767-8, and 833.

#### F.

At the termination of the prosecution's case, and in the absence of the jury, defense counsel started to make a motion for dismissal upon the grounds of the insufficiency of the evidence. The Court ordered the motion made before and in the presence of the jury.

Defense counsel considered the circumstances, and the most unusual nature of this request. It is habitual and customary for such motions to be made in the absence of the jury, for obvious reasons. Secondly, defense counsel considered his very low percent of success the record showed at that time on motions and ruling in that case, upon matters that appeared meritorious. Thirdly, defense counsel noted the intonation and the manner the court used the word "proceed" which looks innocently enough in a cold



record, but when used in the courtroom in the manner of a drill sergeant to a recruit, it left the conception of a positive command; and counsel also noted the court's intonation of other phrases as "There is nothing before the court" which looks innocent also in cold print, but when spoken with inflection implied defense counsel had no valid point and was "bamboozling" the court. After considering these things, defense counsel considered that the court's ruling might appear innocently enough in a cold record on appeal, if a motion were made in the presence of the jury, but it might well be said with such inflections and intonations of the Court as to amount to a directed verdict to convict. The motion was not made before the jury, and was prohibited at the end of the day, before the court in the absence of the jury.

It is better practice to make such a motion in the absence of the jury.

**Upon the Second Trial, the Prosecution refused to call Agent Tormey who was the Principal Investigator, and Principal Witness in the First Trial and who prepared the accounts used by the Government in the First Trial. Defendant was required to call him as an adverse witness and the Court refused to permit the Defendant to examine him as an Adverse Witness.**

Government Agent Tormey was the principal prosecution witness in the first trial. He assisted Agent Krause in the original investigation. Krause went to Sacramento and Tormey finished the investigation, made a report which Krause and Tor-



mey signed; Tormey made the second and third "spreads" resulting in the prosecution accounts, the basis of the first trial. Tormey's conduct of his investigation was a subject of much testimony at the first trial.

At the second trial, he was not called by the prosecution. The defense was required to call him, and did so as an adverse witness under Rule 43(b). Transcript pgs. 558-561, and Suppl. Thereafter all questions as to anything that touched Agent Tormey's vicious acts, or that showed his state of mind toward the defendant, or anything connected with the investigation were excluded upon objection of the prosecution that this witness was the defendant's witness, etc., and upheld as proper objections by the Court.

Examples are questions asking the number of times Tormey saw the defendant after undertaking this case. Tr. 580-1, and Suppl.; if he went to the defendant's place of business in the course of the investigation in the fall of 1946 or spring of 1947, Tr. 582-4 and Suppl.; about the time Tormey brought a blonde girl to the defendant's apartment, Tr. 585-593 and Suppl. Counsel cited the Court to the rule of *Suburban Fruit Lands Co. v. Soderman* 9 Cir. 36 F2d. 934, *Herencia v. Guzman* 219 US 44, 31 SCt. 135, 55 L.Ed. 81, and *Scotland County v. Hill* 112 US 183, 5 S.Ct. 93, 28 L.Ed. 692 and Rule 43(c). He was ordered to desist, and never was permitted to read the testimony of Tormey on direct examination of Mr. Campbell Dec. 3, 1947,

Vol. 7, pg. 655 of the first trial. The objection to this line of testimony was that defendant would be impeaching Government Agent Tormey, her own witness, for bias and prejudice of Tormey and the Court upheld the contention of the prosecution. Tr. 591-4 and Suppl.

Tormey testified differently on the second trial and defense counsel contended that this was hostile acts of the witness. Prosecution counsel objected and the court ordered the remarks of defense counsel to go out. (Tr. 589-9 and Suppl.)

Questions tending to show the account of Tormey, testified to in the first trial, were based upon totals without supporting figures or items was objected to by the prosecution as an attempt to impeach their own witness and that defendant was advancing the government's first trial computations as defendant's correct computations! (Tr. 599-600.) The questions going to what Tormey's account (prosecution used in the first trial) contained were objected to and sustained as immaterial and an attempt to impeach the defendant's own witness. (Tr. 600-1, and Suppl.) Tormey was asked to add the items he gave as a total of \$331, and the items totaled \$277.07. Asked to add these before the jury, Mr. Campbell objected as an attempt to impeach defendant's own witness and the court sustained the objection. (Tr. 605 and 606-7 and Suppl.)

At page 608 of the transcript, counsel for defense, in the presence of the jury, was threatened

with punishment for contempt for attempting to show the government's computations were made up of a series of totals, the items of which had been testified to by Govt. Agent Tormey and whose arithmetical total did not approximate the total testified to by that government agent. Thereafter all objections to interrogations of Government Agent Tormey as to the items were sustained by the Court. (Tr. 608-9 and Suppl.)

Prosecution counsel could not have but known, from the first trial, as demonstrated by the objections interposed, for almost any accounting period involved, that there were figures drawn from thin air, supported by items whose totals did not equal these figures in the government's calculations and account. This type of testimony would prove to any trier of fact the weight to be given to such computations and account. The threat of punishment for contempt in the presence of the jury, and the limitation of the examination was damage and serious prejudice to the defendant's case.

At page 650 to 654 of the transcript, defense witness Beall's testimony relative to the investigation of the government in this case, and showing vicious motives and malice toward the defendant, was wholly excluded.

At pages 811 to 815 of the transcript the defendant was precluded from testifying as to the government's investigation of the case, and Agent Tormey's acts in his official duties in the case.

The prejudice and damage to the defendant by

denunciation of a government agent, precluding the defense the opportunity to obtain the matters going into the denunciation, but merely putting the final conclusions of the government agent into evidence is nothing short of a trial by denunciation well known on the Continent of Europe but unknown to our jurisprudence. The agent took unknown alleged facts determined by him from unknown persons, together with some of the records of the defendant; and these items were put into unknown columns resulting in unknown sums, to which unknown amounts were added and/or subtracted in the so called "work sheets" to give the basic data for Exhibits 28, 29 and 30. We do know that Agent Tormey and Agent Krause used the same basic data, and the same method of accounting (which Mr. Barlow, CPA, and expert for the defendant testified was not a method used by accountants, and which would tend to overstate income). By this method of accounting, the computations of gross-income by Krause were greatly overstated when measured beside the government's first trial accounts and computations.

As Mr. Barlow testified such a method of accounting would overstate income, so the prosecution in both trials advanced figures predicated upon an overstatement by their method of accounting. This could be done to any person engaged in business, for the totals of all money passing through the cash-register, through the bank accounts, and through cash disbursements must of necessity ex-



these rulings and the treating of Agent Tormey as a witness of the defendant, though called by her as an adverse witness, is so apparent as not to require further comment.

**Although often demanded during the Trial, the Defendant was prevented from going into the basis of the Government's computations and accounts, refute the denunciation or show the motive for its institution.**

The prosecution's case was predicated upon the calling of an agent, who testified as to the defendant's alleged income for each of the years covered in the indictment. Then he testified to the difference between these amounts and the amounts computed by government witness Bosserman's computations in the returns, upon which the tax was paid.

Over a dozen separate demands were made by the defense for the basis of these figures—the work sheets from which the government agent testified on the stand. The defense never got them. They were shown to counsel for a few minutes during one afternoon recess, and that was all.

In the first trial, defense counsel was permitted to work for a couple of days with the work sheets of the computations in the account and computations used in that trial. The jury disagreed on the first trial, and the prosecution did not use those accounts or computations again, nor permit the defense to determine the items that went into the totals testified to in the second trial.

Any such practice of building a case upon a



ceed gross income. Distributions of cash were presumably determined by all disbursements shown in the book, plus all discovered by investigation, less those clearly indicated by check payments. The double vice is apparent when certain cash payments and check payments were combined by Krause in his account, to reduce the deductions. When a system of computing income, not used by accountants in their profession, tending to overstate income, cannot be permitted to be put before the jury showing the items used to arrive at the totals, and defense counsel must be refused the right of inspection of the items making up the totals, then such a prosecution case has passed beyond the field of due process, 5th Amendment or the basic concepts of Anglo-Saxon jurisprudence.

Furthermore, the original computations made by Tormey were offered at the first trial by the government as absolutely correct and lawful; yet it differed greatly in almost every respect and item of totals, as for example corrected business income, from the second account and computations made by Krause for the 2nd trial. Yet these denunciations, each claimed by the same counsel in the same case, with the same issues, but at two separate trials, to be absolutely correct and to be accepted without question is the *prima facie* case upon which the judgment of imprisonment, fine, conviction of a felony and brand of criminality is based and predicated.

In addition to this, it appears that Mr. Tormey

was the party making much of the investigation to determine alleged facts from unknown third persons upon which the accounts and computations are based—the basic data, with the exception that Krause had within his withheld basic data, unknown results of inquiries made of some governmental agency, the Bureau of Public Debt. With the exception of this single unknown determination, the same basic data with the same methods of accounting (tending to overstate income) Krause overstated Tormey's figures of business income (corrected) from \$1200 to \$3600 in each of the three years involved.

Yet the prosecution failed to call Tormey as a witness, and it was necessary for defendant to call him as an adverse witness. It was then contended that Mr. Tormey's conduct of his investigation, motives, etc., could not be gone into as the defendant would be impeaching her own witness. If the initiator of the "report" (preliminary denunciation), and principal fact finder of the basic unknown data, Tormey, could have been shown to the jury as a petty employee on his first case who tried to get the defendant to supply an apartment to a blonde girl brought by Tormey, with all attendant circumstances; if the conduct of soliciting an evening including free drinks at the defendant's place of business, and the nature of his conversations and his remarks; and if the other similar matters could have been admitted into evidence as they should

have been, a far different case would have been presented to the jury.

Yet the immediate superior of Tormey who signed the original denunciation (report), Agent Krause, who must justify the official denunciation and the conduct of the investigation made under his responsibility, was not permitted to be interrogated on cross-examination by the defendant as to the conduct of the investigation, nor even as to his participation or knowledge of this phase of the investigation.

The withholding of Tormey as a witness by the prosecution, in view of his connection as the principal witness for the prosecution in the first trial, and his activities as principal fact finder for the basic data used in the suppressed "work sheets", should evidence the depths to which the prosecution sunk in its conduct of the case, and by itself is grounds for reversal.

Certainly the motives of this denunciation, these computations, are the proper subject of evidence in the case at bar. One of the proofs of motive is not the testimony of a biased and witness who should be fearful of dismissal for misconduct, that he has no malice; but the acts, words and conduct of Tormey during the actual fact finding which was the basis of the unknown items in the unknown computations is the only reliable testimony. There was every reason for Tormey to do harm to the defendant which he did by his misrepresentations against the taxpayer. There was every reason for

Krause to cover up his responsibility with a conviction by putting these unknown figures into unknown columns to reach a result to justify his original report signed by himself and Tormey. Certainly the great divergance in figure which were the basis of his computations, summarized in Exhibits 28, 29, and 30 showed such divergance in both corrected business income and other income from that made by Tormey (using the same basic data and same method of accounting likely to overstate income), should justify an inquiry as to what items went into what columns, that were the difference and/or sums resulting in the figures going into those exhibits. Certainly these discrepancies were enough to cast the gravest doubt upon the motives of those making the alleged account and computations—the denunciation which is the basis of the instant case.

Any person, no matter how honest, can be convicted upon such a trial by denunciation. A petty government employee no matter what his motives (so bad as proved on the first trial that the prosecution would go to any ends to keep them from the jury), can submit a denunciation that the taxpayer made certain income in excess of his reported income, and set shocking figures and allegations in the denunciation, the first of which is the “report”. These are reviewed and presumed true. The wheels of the Penal Division and the Department of Justice are started turning against the taxpayer, solely on this original denunciation. Presumably,



the denunciation alone is presented to the Grand Jury and the indictment follows. At the trial, the petty employee testifies he computes the income at such and such a figure (by a method likely to overstate income). The taxpayer can ask the methods of how he handled this or that item. The taxpayer demands to know what is in the columns making up these inflated and overstated figures, particularly income. The bill of particulars is denied. The prosecution contends there are thousands of items in the "work sheets". The "work sheets" are demanded for examination, and refused; demanded as evidence, and denied. There would be no way to prove the taxpayer is innocent of the denunciation, except to testify to a mass of detailed transactions; so whenever a strong point is to be brought out (and particularly if the prosecution knows them before hand, it being a re-trial) an objection is interposed and no matter how weak or illfounded, it is sustained. While the accused is proving the defense, the trial judge insists the trial is lagging and insists the defendant's counsel is wasting time—nine times—so the jury has the impression it is not material nor worthy of consideration. What chance would any taxpayer have in such a position? The denunciation is the basis of the prosecution and their case. It is that denunciation which follows through to the stamp of the felon, the judgment of conviction and the sentence of fine and imprisonment and the degradation of a convicted criminal. If this is permitted under our jurispru-



dence, "trial by denunciation" has become a reality in this great nation, and due process, the requirement of an indictment by a grand jury, etc., are but empty phrases in the Constitution.

**A Bill of Particulars was timely requested. It was denied.**

**The Defendant was surprised and the Items of Account in the Prosecution Account and Computation was refused inspection by the Defendant or to be put into evidence though repeatedly demanded.**

The defendant's counsel worked diligently in the preparation of the instant case. No method of accounting nor estimation upon the facts provided by the defendant would approximate the figures charged in the indictment, but more nearly approximated the returns of the defendant.

It was apparent that Bosserman in preparing the returns had omitted many deductions the law provided. It was also apparent that although Bosserman knew of the income from the claw machine, pinball and juke box, and the deposits of the defendant in her commercial account, he had merely totaled the cash register totals of bar sales and made up the returns on them as the sole source of income. Yet the cash checked out of the bank, including income other than bar sale receipts, went for the most part to business expenses. Thus as other unreported income appeared, so did unreported deductions, and the final results closely approximated the income on which tax was paid.

Counsel for defendant had at his disposal only some of the cancelled checks, bank statements, book

of account, miscellaneous receipts and the recollection of his client which covered numerous transactions over a three year period. Many of these matters had been handled by agents and employees of the defendant. Her recollections were those of a woman who knew little of business and who had relied on others in many instances and whose memory for detail was at best hazy after the passage of five or more years.

Several informal discussions were held between counsel for the defendant and the Government counsel and agents in which it appeared that there were income and deductions determined from investigation and examination of books of those who dealt with the defendant in 1942, 1943 and 1944 which did not appear in the books or records of the defendant.

A demand was made for a bill of particulars to discover what these various items were that made up the income and deductions that resulted in the mathematical difference between business income and expenses to be the item "net income from bar" charged in the indictment. It was refused. So an affidavit of counsel for the defendant in support of the demand for bill of particulars was filed, setting forth substantially the above facts and circumstances. Along with it was the affidavit of defendant herself setting forth these facts and her inability to supply her counsel with this data and information.

Upon the motion hearing, Mr. Siegel, assistant

counsel in the penal division, testified that all the computations were based on matters within the defendant's records. (Tr. of Sept. 2, 1947)

The motion for the bill of particulars was denied.

Upon the first trial, Mr. Tormey, a government agent who made the investigation for the most part, and the person making the computations, testified as the principal government witness.

Defense counsel was permitted to work for a couple of days during the first trial upon the work sheets and to go at length into these matters, particularly the deductions. Defense counsel showed these computations in their true light, together with the facts of Mr. Tormey's investigations which shed light (or we might say a dirty shadow) on his personal motives and malice toward the defendant.

It was not until the fourth day of the second trial, March 26th, Transcript Pgs. 322-323, that defense counsel learned a new and separate and different computation had been made and new and different income sought to be proved against the defendant.

The prosecution found from the first trial and cross-examination of their agent Tormey that the charges against the defendant could not be substantiated by their accounting. They knew that if the defense counsel could find what items made up the totals, they had a case that could not convince a jury, in the face of cross-examination and the defendant's testimony.

The only possible reason for refusing a bill of particulars and opposing a motion for a bill of particulars was to surprise the defense and to preclude the showing to the court and jury by defense of the errors, falacies and omissions in the prosecution's computations and account.

The prosecution knew the weakness of its case. They therefore caused a new and separate account to be prepared and to give the defendant some of the lawful deductions proved at the first trial. To show a taxable income, this second computation using the same basic data and the same method of accounting inflated the "corrected business receipts":

1942	Ex. 28 (Krause)—Corrected Business Receipts....	\$15,388.48
	Agent Tormey, first trial computation, Tr. 579....	13,941.59
	Inflated by.....	\$ 1,274.75
1943	Ex. 29 (Krause)—Corrected Business Receipts....	46,506.45
	Agent Tormey, first trial computation, Tr. 571....	44,187.65
	Inflated by.....	\$ 2,318.80
1944	Ex. 30 (Krause)—Corrected Business Receipts....	54,004.50
	Agent Tormey, first trial computation, Tr. 569....	50,342.45
	Inflated by.....	\$ 3,651.85

This was enough to put any reasonable person upon notice that these second trial computations were wrong; that one need only find what items that went into these second figures, to show the Court and jury that there was no tax at all, and there was no case.

Defense counsel requested of the government



counsel the right to inspect these items that made up these ultimate figures testified to by Agent Krause. He had these in so called "work sheets" in which each item was entered and each computation made for the ultimate results entered as beginning totals in Exhibits 28, 29 and 30. This was refused defense counsel. Demand was made to the Court for an order to produce them more than a dozen times. The defendant did not get them.

A.

The defendant stated to the Court at Transcript Pg. 350 that Mr. Krause's testimony of a separate and subsequent accounting and computation had caught him by *surprise*:

Tr. Pg. 350. "Mr. Campbell: You may cross-examine (Mr. Krause).

Mr. Crittenden: If your Honor please, this has caught me by complete surprise. There are a number of things he has covered in his direct examination in connection with his computations that are much out of line with the former computations and testimony we had. Your Honor will remember—

Mr. Campbell: If your Honor please, I object to this, I think this is highly improper.

Mr. Crittenden: I have to go into those questions.

The Court: You may bring those matters up in the absence of the jury. You may proceed with the cross-examination.



Mr. Crittenden: Q. Mr. Krause, you were here during the last trial, weren't you?"

\* \* \* \*

It appears on Transcript Pages 322-323 on voir dire questioning of Mr. Krause by the defense counsel:

Mr. Crittenden: I understood that Mr. Tormey made all the computations after your first. He made the second and third spread, isn't that correct?

Mr. Campbell: I object to that question. That is not a voir dire question. This man has shown his qualifications. I have no objection to any questions as to this man's qualifications as an accountant.

Mr. Crittenden: He has not made the computations.

Mr. Campbell: He stated he has.

The Court: You may take him over on cross-examination and ask him any question you wish.

Mr. Crittenden: Your Honor remembers the testimony at the former trial. Mr. Tormey is the one who made the computations.

The Court: You may develop that on cross-examination.

Mr. Campbell: Q. You made this audit, did you, Mr. Krause?

A. I personally made this examination to which I am testifying.

Q. When did you complete it, Mr. Krause?

A. The audit, here, oh, about a week or two ago.

\* \* \* \*

B.

It was not until almost the end of the second trial that it was learned from the testimony of Agent Tormey that the figures of the Government were not confined to the defendant's records and papers, but included other matters.

Mr. Tormey testified, Transcript 572, that Krause obtained information outside the record.

“\* \* \* In this case, in Mr. Krause's audit, he got authentic bond records from the Bureau of Public Debt, which shows that she had purchased bonds for cash, although not shown in her books or in her checks, or by withdrawals from her bank accounts, and he consequently added those amounts as unreported income, which accounts for the fact that his income figure is greater in one year than my figures.”<sup>1</sup>

At Pages 621-2 of the Transcript, Mr. Tormey testified that the figures in the Government's computations could not be obtained from the defendant's books and records in evidence. Other matters determined by the investigators, outside the books and records in evidence went into the accounts of the prosecution.

At Page 640, the *surprise* of defense counsel and

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<sup>1</sup> It should be noted that during War Bond drives, the Defendant bought and gave to winners by chance some war bonds to customers. This would account for these bond purchases, but they would be a cost of doing business and not income for her, for she disposed of them to customers.

the testimony of September 2, 1947 by the attorney of the Penal division having misled him, is shown:

“Mr. Crittenden: I have a question or two. I want to state to the Court before I start in that I am greatly surprised in this: At the time we asked for a bill of particulars, particularly on September 2, 1947—

The Court: Just a moment. You proceed with this witness. I am not concerned with what you have in mind. This witness is on the stand. Examine this witness and proceed to do it now.

#### Re-direct Examination

Mr. Crittenden: Q. Mr. Tormey, you say the ordinary audit requires external verification in addition to the books and records?

A. Wherever it is possible.

Q. You go out and made an independent investigation?

A. It is left to the judgment of the investigating officers.

Q. You go out and make independent investigations?

A. Oh, yes, we check bank accounts, we check the accounts of vendors or wholesalers or department stores. That is customary procedure.

\* \* \* \*

Q. And you in making up accounts rely on this external investigation as part of the audit?

A. If it lends itself to being proved, it seems reasonably, if their records are kept in normal

business affairs and the people responsible will testify that they are correct, we certainly do as to them.”

At page 646 of the Transcript the surprise and misleading of defense counsel was put into the record.

B.

Counsel for defendant was faced with a new, different and unrelated evidence by Agent Krause of another income than charged in the indictment and different in every respect than the evidence in the first trial, except it was presumably computed by the same accounting method from the same basic data. The alleged corrected business income and alleged other income and alleged deductions and expenses were different.

Request to see the work sheets, the supporting documents for Exhibits 28, 29 and 30 was made by defense counsel of the counsel for the prosecution during the noon hour recess the day Krause and the prosecution sprang the new accounts. It was refused.

While Krause was still on the stand as a witness for the government, demand was made in open court, an order was requested of the Court for permission to examine the work sheets, and a request was made for an order to put them in evidence. (Transcript 447-452)

The requests were denied.

The defense counsel was permitted to look at the work sheets of Krause for the ten minute



afternoon recess, glancing from January to May 1933 very hastily. (Transcript 455)

At the start of the morning session of March 31st, defense counsel reported to the Court that he had not yet had an opportunity to examine the work sheets of the Government's current account and figures, except for the few minutes at the afternoon session recess. Transcript 478. Counsel for the defense requested the papers, from which Mr. Krause testified, be introduced into evidence. Mr. Campbell told the court it would be available when Mr. Krause arrived and the court ruled it would be available.

At the end of the morning session on March 31st, demand was made of Government counsel for the work sheets showing deductions allowed and how the income was arrived at. It was denied.

At the commencement of the afternoon session of March 31st, counsel in open court reported the demand and stated he had not seen them. The court ordered defendant to proceed with the case. Transcript 531.

At the end of the day's session on March 31st, defense counsel requested an order to enable him to examine Mr. Krause's records from which he testified. The court observed he has never known the government to withhold information within reasonable bounds. Counsel for defense stated to the Court it was not true in this case and asked for work sheets showing disallowed items, those showing deductions allowed and the work sheets show-



ing the far greater income than computed by Agent Tormey. The Court observed if he went into the work sheets the jury might become uneasy and he didn't see how it could be done and adjourned. Transcript 594-595. We might note that a jury trial is not like the legendary justice of the peace who only permitted one side to argue a case because when he permitted both sides, he became so confused he had a hard time making a decision.

On Transcript Pages 527-8 defendant requested Mr. Krause's work sheets for handwriting comparison as an exemplar. Request for an order to deliver work sheets lying on the table in open court was denied.

On the morning of April 1, 1948, counsel for defendant on Transcript Pages 646-7, stated the surprise of learning that the government's figures involved matters determined by outside investigation by the government agents and not confined to the records and books in evidence contrary to the sworn testimony of government Attorney Siegel on September 2, 1947; which would have been apparent from the "work sheets" of Krause if put into evidence and counsel again stated he had asked for these accounts. The Court refused them.

On April 2nd, during defendant's attempt to prove the various larger items of expenses, Counsel for the prosecution contended Krause had allowed all items of expense for business entertainment. Transcript 724. Defense counsel stated he did not believe that was a fact, that the exact figures were

demanding as to what was allowed and what was disallowed and it had been refused. The Court thereupon instructed the jury to disregard arguments of counsel and ordered the case to proceed. Obviously some deductions somewhere had been disallowed, by an examination of the total deductions testified to by Krause and the items appearing in the defendant's books and records. The items allowed and disallowed in the Krause computations remained and still remain a mystery, despite every effort of the defendant to determine them during the trial.

At Transcript 755, defendant attempted to testify as to certain expenses attendant with the business operations.

The Court remarked that he was not concerned with the services performed by the defendant's sister who was brought to California in 1943 to assist with the business. Defendant sought to show the travel expenses of the sister were connected with and deductible as a business deduction. Mr. Campbell stated they were allowed. Defense counsel stated he had no way of knowing they were allowed, that consistent demands were made to see the Government's papers and they were seen by counsel at but one recess on one day. The Court thereupon recessed the trial to handle other matters.

### C.

The items of "net income from bar" and "rental income" as charged in the indictment are ob-

viously the mathematical differences between unknown items totaled together as gross income and unknown items totaled together as deductible expenses, depreciation, losses, etc. The ultimate difference known as "net income from bar" and "rental income" thus, does not appraise the defendant of the nature of the charges, nor of the proofs nor whether additional income is sought to be charged to her, nor whether certain deductions are claimed as disallowed, or another base or rate of depreciation is sought to be proved, on any or combination of these matters.

The prosecution then brings in proof by its witness, an agent investigator, who testified he computes the defendant's income at a certain figure and deductions at another figure whose mathematical difference is different from that charged in the indictment by a substantial proportion.

Upon a second trial, on the fourth day, another investigator agent takes the stand and testifies to a substantially different and separate set of figures. Obviously if the same basic data and same method of accounting were used, such substantial differences and increase in gross receipts would require an analysis and investigation into what items went into these totals. Demand to inspect the papers from which the witness testified and demand to produce them for evidence were first recognized as valid, then met with passive resistance and finally wholly denied.

Near the end of the trial it was learned that

these figures of the Government were not confined to records and books of the Defendant but were based upon investigation.

This is a trial where an agent testifies that he has investigated the defendant and finds her guilty. Asked as to the factual matter of his conclusions and what goes into it, it is refused and the court sustains the refusal.

The denunciation of the accused by the government agent based upon unknown series of alleged facts, from unknown investigations and unsworn statements of unknown third persons is the *prima facie* case. The defendant wishes to prove facts in her defense and the government contends the investigator has considered and allowed these facts to arrive at his conclusion.

Gone is the constitutional prerequisite of due process, Fifth Amendment, U. S. Constitution. Gone is the requirement of an indictment sufficient to appraise the defendant to prepare her defense and to cross-examine the witness or government agent against her. Gone is the requirement that these unknown parties giving *ex parte* oral or documentary testimony of receipts and disbursements to the investigator, shall confront the accused, be sworn and subjected to cross-examination. Gone is the right to put on a defense. The denunciation of the government agent presumably initiates the trial and charges and suffice to convict. "Trial by denunciation" is no longer a term confined to a tyranny in Continental Europe but a



reality on our jurisprudence. Woe, to the unhappy taxpayer who does not provide an apartment for the agent's blonde female associate! Woe to the unfortunate citizen who crosses a petty Internal Revenue agent. He or she will be denounced and the denunciation will be the stamp that results in conviction of a felony, fine, imprisonment and disgrace and disability of a convicted criminal.

E.

Defendant in the case at bar, is in a similar position to the defendant in *U. S. v. Empire State Paper Co.*, (DC NY) 8 Fed. Supp. 220 where each was confronted with alleged correct figures in the income tax evasion indictments, and there the court said, in granting a motion for a bill of particulars:

“The difficulty of the defendants in their defense appears to have arisen from the fact that the figures set forth in the indictment as going to make up the true income of the defendants are not to be reconciled with the books of the defendants to which they have always had access. Counsel for the government admits the computations which appear in the indictment are not made up of figures taken from the books of the defendants. The defendants are, therefore, in the more or less difficult situation of being confronted with an aggregate amount set forth in the indictment from which a true return should have been made without knowing in advance of trial what details have been used by the government expert accountants in making up these gross figures. As it appears to me, this will be a situation most embarrassing to the defendants upon the trial, and in addition of placing them



in a position lacking entire opportunity to prepare defenses for the charges embodied in the indictments as to the source of receipts and expenditures with which under the statement of counsel for the government they are entirely unfamiliar.”

The purpose of an indictment is to inform the accused sufficiently of the facts constituting the alleged offense to permit her to prepare her defense, to advise her counsel of the facts to permit a defense, intelligent cross-examination of government witnesses and to enable the defense to test and rebutt their testimony; to permit the Court to determine the issues and to rule on the admissibility of evidence, and to permit a plea of res judicata upon a final determination of the proceedings.

As the indictment stands, without the required information by the bill of particulars, the defendant did not have and does not now have the slightest notion or idea of what sum or sums, or from what source or what items went into the charge against her, or what deductions and what items went into deductions to arrive at the “net income from bar” or “rental income” in the indictment; or for that matter what went into the figures to arrive at the various starting figures in Exhibits 28, 29, and 30.

Although the indictment in each count states “Gross Income”, it expresses all figures under them as “net income”. It is elementary that a figure of gross income for each year must have

been arrived at and certain expenses and deductions subtracted from that figure to arrive at certain figures alleged in the indictment as “net income from bar”, etc. The taxpayer defendant could not commence to examine and compare her figures in her book and records against those charged in the indictment until she knows what gross receipts she was charged with having received and what expenses and deductions have been allowed in arriving at the figure in the indictment.

As the Court stated in *U. S. v. Empire State Paper Co.*, (DC-NY) 8 Fed. Supp. 220, in granting the motion for a bill of particulars in an income tax evasion indictment:

“The Court has in mind from observation and experience in income tax cases, that the figures of expert accountants even from the same department often vary greatly in conclusions arrived at, so that it is frequently most difficult for the taxpayer not skilled in the art of expert accountancy to ascertain what a specific charge, either civil or criminal, may be on the part of the government.”

So in the case at bar, there are any number of items upon which we dare say, not two certified public accountants skilled in personal income tax work would agree on every item, having been added together in total figures; and from that total figure, another column of figures or items, even more subject to disagreement by even such skilled accountants, had been deducted. The conclusions thus arrived at are the “net profit from bar” and “rental

income” which are the alleged ultimate “facts” of the indictment, added together to become “gross income” in the indictment.

If the accused were guilty, and had received the monies sought to be charged to her as evaded income, she might be presumed to have known the various transactions of her business, whether conducted by her personally or through agents, servants and attorneys, even though taking place up to more than five and a half years before.

If the defendant were guilty, and she is entitled to the presumption of innocence during the indictment and up to the time of judgment, she cannot know, suspect, nor imagine what the elements of the offense stated in the indictment could be—until surprised by the proof at the time of trial. She cannot know the gross receipts she is charged with receiving, until surprised at the trial, and then not the items attempting to make up that item. She cannot know the deductions and expenses she may be credited with in arriving at “net profit from bar”, except to be surprised at the trial with a lump sum figure and never permitted to find out the items going to make it up, to know which were omitted or disallowed. The indictment merely charges the mathematical difference between the sums of these two. To charge the defendant with knowledge of this alleged offense, is to determine her guilty before trial.

Such a rule as contended by the government in it offered bill of particulars that the elements of the offense are within the knowledge of the defendant is to end the requirement of the Fifth Amendment United States Constitution that an indictment must be presented against a person. So an accused charged with murder, cannot complain of the failure to name any of the details or facts, for the defendant is presumed to be within the possession of the facts or means of determining or ascertaining the particulars including the name of the alleged deceased, the time and place of the offense, etc. A person charged with larceny is in the possession of the means of ascertaining the particulars—the time, place, ownership, nature and extent of the property involved, by reason of the fact that the defendant was present and knew these facts and has the loot from his wrong. See Ninth Circuit decision of *Foster v. U. S.*, 253 Fed. 481.

It was stated in *U. S. v. Allied Chem. & Dye Corp.*, (DC-NY) 42 Fed. Supp. 425, in granting a bill of particulars:

“One indicted of a crime is presumed not guilty and that he is ignorant of the supposed facts upon which the charges are founded . . .”

In an income tax evasion case, when it appears that the indictment does not inform the defendant with sufficient particularity the defendant is entitled as a matter of right to a bill of particulars.

The Third Circuit in *Singer v. U. S.*, 58 Fed. 2d



74, in holding that a conviction for wilful evasion of an income tax be reversed, held:

“When it appears that the indictment does not inform the defendant with sufficient particularity of the charges against which he will have to defend at the trial, he is entitled to a bill of particulars, if seasonal application is made therefore. The Defendant may demand this as a matter of right, even though the indictment sets forth the facts constituting the essential elements of the offense with such certainty that it cannot be pronounced bad on a motion to quash or demurrer; where the charge is couched in such language that the defendant is liable to be surprised or unprepared. *Tilton v. Beecher*, 59 N.Y. 176, 184, 17 Am. Rep. 337; *Watkins v. Cope*, 84 N.J. Law 143, 147; 86 A. 545; *State v. Bove*, 89 N.J. Law 350, 353, 116 A. 766; *United States v. Eastman* (DC) 252 Fed. 232; *Wilson, et al v. United States*, 275 Fed. 307, 310 (CCA-2); *Bodine v. First National Bank of Mercantville* (DC) 281 Fed. 571; *Filatreau v. United States*, 14 F. 2d. 659 (CCA-6); *Lett v. United States*, 15 F. 2d. 686 (CCA-8); *O'Neill v. United States*, 19 F. 2d. 322, 324 (CCA-8).”

The Court in that decision pointed out prejudice suffered by the defendant from the mass of irrelevant and prejudicial evidence admitted for failure to require a bill of particulars; and the surprise and prejudice suffered by the defendant from the failure to require a bill of particulars. It was also commented upon that a defendant could not remember details of financial transactions after five years (a comparable time in the case at bar).



The Ninth Circuit in *Maxfield v. U. S.*, 152 Fed. 2d. 593 said:

“It is claimed that the Court was in error in denying appellant’s motion for a bill of particulars; and *Singer v. United States*, 3 Cir. 58 F. 2d. 74, is relied on as authority. In the *Singer* Case the indictment failed to distinguish net from gross income; and the accused were surprised by the government’s evidence to the extent that long recesses had to be granted on several occasions. There, also, the books of the accused were in the hands of the government and were withheld from the use of the defendant.

No comparable situation existed here. . . .”

In the instant case we have the elements of the *Singer* case, and the elements missing from the *Maxfield* case: In the case at bar the indictment confuses “gross income” and “net income” placing “net profit from bar” as an item of “gross income”. We have the element of surprise. We have two separate, distinct and different accounts offered by the prosecution, one at the first trial, and the springing of the second computations and accounting in the second trial in its fourth day. We have the partnership book in the hands of the government. In addition, we have unknown items, from unknown third person’s records, determined by an investigation from which all testimony was restricted on cross-examination as to the investigation, its conduct, and extent. These items make up part of the income, and presumably part of the deductions in the government’s second account and

computations, in addition to unknown items of alleged bond purchases determined from inquiry of some government bureau, which are expenses of business and not income.

The substantial variance between the allegations and the proof are certainly not the differences covered in the Maxfield decision. The indictment charges as an item of "income from bar" as an item of "gross income" in the indictment the sum of \$2,785.92. Krause in Exhibit 28 sets up net income of the business at \$172.13. This is the sole count upon which a verdict of guilty was returned, and upon which the judgment appealed from is predicated.

The obvious reason that the prosecution refused the bill of particulars, was that it was calculated to surprise the defense. It did. On the second trial, on the fourth day of taking testimony, the prosecution brought forth a new and different contention based upon a new and different account and computations. Obviously, it was intended to surprise the defendant, having offered another and separate account and computations as the absolute truth at the first trial. The prosecution refused the defense the right to inspect the work sheets to determine what went into these items, for they knew it could not stand searching analysis or adverse inspection. The prosecution refused to put the work sheets in evidence, because if the jury should see what made up the items or the computations of the Krause figures, it would discover the

fallacies, errors and omissions of the computations. Any method of accounting, not used by certified public accountants, and likely to overstate income, which upon the same basic data would result in such greatly different "corrected business income" as shown by the two government's agent accounts and computations, cannot stand the scrutiny of the defense nor of the jury.

There is no good reason why the various items making up the alleged "net profit from bar", "rental income" and allowed deductions should not be furnished the defendant, by a bill of particulars, upon timely demand. Those that are admitted correct need not be gone into by the defense. Those that are improper can be made the subject of issue in the trial. Disallowed deductions are known by those that were omitted from the allowed deductions, and the issues are narrowed. The defendant will not be surprised. Methods of computation appear at once, and where they overstate income, can be shown to the jury. The only reason for withholding is that they cannot stand the test of examination, and must be withheld, and the totals sprung as a surprise to the defendant.

By this withholding, the trial lacks the essence of fair play, and the defendant must go into the details of the three years of various transactions, unless precluded by the court from putting in this defense. Any tax income trial, without such a bill of particulars, becomes a trial by ordeal, in which sheer weight of the defense means financial ruin,

regardless of the outcome. Unless one has been fortunate enough to have considerable liquid assets, one must forego the expense of a detailed audit by certified public accountants as proof in the defense. The defendant, unfortunately, did not fall within the classification of one who could afford such an expense. If she had been guilty as charged, she might have had the means to employ certified public accountants for such a detailed audit. Tax liability in matters of considerable importance and complexity are tried in a matter of hours before the United States Tax Court by a narrowing of the issues through the tribunal's procedure. The new Federal procedure permits the reduction of a cause to its real issues. See Federal Criminal Rule 7(f) and the note under it "This rule is substantially a re-statement of existing law on bill of particulars".

The defendant merely asked for the items making up the amounts charged as "net profit from bar" and "rental income", and items making up deductions of business expenses and deductions. It is absurd and preposterous to expect the defendant to prepare for a trial with less, in view of the showing for the bill of particulars, or for the court to determine the issues and the relevancy of the testimony without it.

We note merely as a matter of interest that the present English criminal procedure requires that a witness not called at the preliminary hearing, cannot be called as a witness for the prosecution



without the defendant being properly informed of the expected testimony. Nor in the Continental Law countries is a defendant surprised, for each witness is thoroughly interrogated in the presence of the accused by the Judge d'Instruction prior to the trial of the accused. Certainly, our system of jurisprudence is not calculated to surprise the accused at the time of trial.

Defendant is entitled to know exactly the nature and extent of the crime of which he is accused, and where the indictment is substantially good, but it appears the defendant cannot properly prepare his defense without a bill of particulars, the Court will order the prosecution to furnish it.

31 *Corpus Juris*, page 750, Indictment & Info. Sec. 308. It was said in *U. S. v. Allied Chemical & Dye Corp.*, 42 Fed. Supp. 425:

“A bill of particulars will be ordered whenever it appears to be necessary to enable the defendant to meet the charge against him or to avoid danger of injustice. *Coffin v. United States* 156 U.S. 432, 15 S. Ct. 394, 39 L. Ed. 481. If the indictment is couched in such language that the accused is liable to be surprised by the production of evidence for which he is unprepared, he should apply for a bill of particulars. *Rinker v. United States* 8 Cir. 151 F. 755, 759 . . .”

The Ninth Circuit stated in *Perez v. U. S.* 10 F. 2d. 352, where objection was made to the sufficiency of the indictment:

“If further information as to the details of the charges were desired by the plaintiff in error, he had his remedy by applying for a bill of particulars.”

The Ninth Circuit in *Shaw v. U. S.* 131 F. 3d. 2d. 476, involved an indictment for sending unregistered securities through the mail:

“If the accused, for purposes of his defense, desired a more particular detailed description of what persons were engaged in the process of carrying through the mails, he should have moved for a bill of particulars.”

The Supreme Court in *Kirby v. U. S.*, 174 U. S. 47, 19 S. Ct. 574, 43 L. Ed. 890, involving an indictment for receiving stolen property (stamps) said:

“If it appears at the trial to be essential in the preparation of a defense that he should know the name of the person from whom the government expected to prove that he received the stolen property, it would be in the power of the Court to require the prosecution to give a bill of particulars.”

As the case turned out, the government attempted to prove a far different offense than the one charged in the indictment. It is considered a basic concept of criminal justice, as well as a basic concept of fair play, that the proof at the trial should substantially approximate that charged in the indictment.

This is not a case like that of *U. S. v. Skidmore*, 123 F. 2d. 604, where a bill of particulars is sought solely for calculations upon matters admittedly confined to the defendant's books, for here it was shown by the affidavits in support of the motion for a bill of particulars that no matter what methods of computation or estimation were used, the income

from the defendant's book and records more closely approximated the reported income of the defendant and not the income alleged in the indictment. Indeed we should note that the government's proof in the Krause computations suffered from the same vice; yet the Krause computations are based upon "basic data" not confined to the defendant's book or records.

**Much Admissible Testimony was excluded during the Trial.**

1. The divorced husband of the defendant was called by the prosecution as a witness. The prosecution contended that although the parties lived together from their marriage in March, 1942, to their separation in July, 1943, that there could be no community property from the earnings of the parties during the marriage, though residents of California. In 1943 there was an action for divorce filed in July by the defendant alleging no community property in the complaint; a default, and the interlocutory decree was silent. The divorced husband sought to set aside the default, and consulted counsel, and verified a pleading claiming community property. The question as to the contentions of the husband and his claim of community property on the proceedings to set aside the default was excluded upon objection of the prosecution. Transcript 174-175a, Suppl.

2. The prosecution called a disgruntled former bartender of the defendant to testify as to amounts of sales on several big days; he claimed he counted

the cash in the cash register at the end of the day. At the first trial he had testified to having drunk about 20 regular drinks of bourbon whiskey each day he was working for the defendant as her bartender. To bring out the condition of the witness at the end of a day, and to permit the jury to understand the weight to be given to such a witness' testimony, he was asked as to whether at the time he testified he drank during the day, and he testified he did. The prosecution objected to the question as to the number and amounts of drinks and the court sustained the objections. Tr. 204-6, and Suppl.

3. The prosecution witness Shannon testified as to the two periods of employment—the first trial he said the former period ended in 1943 and in the second trial, he placed it all in 1942. He testified that the biggest daytime sales was \$142, a day shift, during a “wake at Dugan’s”. To impeach the witness' veracity, he was asked if the wakes were held during the day or night (for the night was the time of larger volume of bar sales, and wakes are held at night). The Court precluded this line of questioning. (Tr. 196-7 and Suppl.)

4. The Witness Shannon testified as to volume of sales from money in the cash drawer of the register. Defendant was interested in showing that the amounts Shannon testified to was the gross sums and including the opening amounts of \$25 to \$50 which should be subtracted to arrive at



actual gross sales. This cross-examination was not permitted. Tr. pg. 203, and Suppl.

5. The testimony of prosecution witness Washauer of the Internal Revenue Bureau on direct examination was that the investigation started as the result of an "anonymous letter". (Tr. pg. 19.) On cross-examination it was brought out that the letter was signed by some name (Tr. page 27); however, the witness claimed there was no such person as the name signed (Tr. pg. 28). The defense demanded the original as the signature might be misunderstood or the copy not a correct one (Tr. 27-8). The next morning, the letter was produced, but the court sustained the prosecution's objection it was privileged (Tr. 85-8) and suppl.) and the document is among the exhibits on appeal in a sealed envelope. If it were an anonymous letter as the prosecution contended, it would not be a privileged communication, for the identity of the informer would not be disclosed; and there is no contention that the fact of the obtaining of information from some unknown informer is privileged, nor the nature of the information. The evidence suppressed must be presumed to be adverse to the defendant.

6. Government Witness Bosserman was an accountant who solicited the defendant's accounting business, was hired by her to prepare her tax returns, who took her records and prepared the returns which she relied upon. These are the subject to the three counts of the indictment. On cross-

examination the witness testified he threw out a number of deductions in computing the returns which she could have taken. Asked if he had given the government the breaks in making out the returns, objection was made that the cross-examining counsel was putting words into the witness' mouth! And the objection was sustained. Tr. 222-4 and suppl.

This is just what a leading question is, and permissible on cross-examination.

7. Bosserman testified on the second trial that he computed the 1942 partnership return from the "Gray Book", although on the first trial he had testified he had not used the "Gray Book", and before the first trial had conferred with defense counsel in their office about the returns and the "Gray Book". On cross-examination Bosserman was asked about having said he had not seen the "Gray Book" and the prosecuting attorney objected as the cross-examiner is putting words in the mouth of the witness! The objection was sustained (Tr. 249 and Suppl.). Certainly leading questions by defense counsel of a hostile witness are permitted, and recognized as proper.

8. Bosserman was asked on direct examination about his informing his accounting client that gambling winnings were taxable, and the alleged conversation. At the first trial Bosserman had testified that such a conversation was not had until late in 1945, and defense counsel showed the transcript of the testimony and the witness testified he

believed he did so testify. Thereafter the prosecution objected to any questioning about the defendant's reply that she was surprised to find it was taxable; to permitting the witness to explain; or to reading into evidence of the prior testimony that was inconsistent. All of this the Court sustained. Transcript 252-4 and Suppl. Impeachment of Bosserman's testimony that the defendant told him nothing about the income from the machines was also prevented, by prior testimony at the first trial was objected to and some objections sustained, and the court refused to make a ruling, ordering defense counsel to proceed. Transcript 255-8, and Suppl.

9. The letter written by Bosserman to defense counsel before the first trial that the client did not have the slightest idea of income tax or what was taxable and what was not; showing complete reliance upon Bosserman's professional services in the tax returns in the case was offered, the signature proved by the writer, Bosserman. Upon objections of the prosecution, its admission was refused by the Court. Bosserman had testified that the defendant had not disclosed to him her reliance upon him and his knowledge that she had no concepts of income tax, and the letter of the accountant was offered for impeachment of this testimony of Bosserman. It was also offered to show that the defendant relied upon his professional services and acted in reliance on them, and he knew it. This letter was marked for identification, Exhibit C.

10. The defendant alleged in her complaint for

divorce in July, 1943, that there was no community property on that date. Soon after she acquired the full interest in the bar business on July 16, 1942, her husband left his job with the Dacus Oil Co. and spent full time working on the bar. The Prosecution computation showed that the net income from the bar for the period of July 16, 1942, to the end of 1942 was \$172. To show that there had been and was community income, but much of it spent up to the time of the divorce, so that the allegations of the complaint would not mean that there was never any community income during the status of marriage, defense counsel asked the defendant as a witness what property she had at the time of the separation from her husband in 1943. She testified she had her car and her business, some money in the bank and owed some bills. She was asked the approximate amount she owed at this time; it was objected to and sustained. Transcript 761. She was asked if she discussed the allegations of community property in her divorce complaint to her lawyer, Mr. Hyman. It was objected to and sustained. Tr. 761. A series of questions as to the community property allegations, the divorce, etc., and the advice of her counsel as to the effect of her allegations when she brought the divorce action were all sustained. Tr. 762. The doors to any defense or effect of the community property law or the income of the husband to be charged against him and not reportable by the defendant wife, particularly in the year 1943 when



separate returns were filed, were closed to the defendant.

11. The defendant gave a rough guess inventory to the government agents during the investigation, prepared for her by others. The Government offered this "best guess at the time", made more than a year after, as proof of actual inventory. A question to bring out how and who made the alleged inventory, to give the facts upon which the jury must determine how accurate it was and what weight should be attached to it, was objected to by the prosecution, and the court sustained the objection. Tr. 819.

12. The prosecution, in an effort to prejudice the jury against the defendant, went into great lengths about entries in the year 1944 books of gambling losses, as gifts to Red Cross, Good Causes, etc. The defendant took the standard deduction of \$500, which was allowed regardless of the amounts given for charities, losses or other deductions. It would not make the slightest difference in this case that gambling losses be entered as charities, if the tax showed the losses deducted from gambling winnings. Rather than to defraud the government, the taxpayer by doing this would be injuring herself. With the standard deduction taken, entries of gifts to charity are mere surplusage. There being gambling winnings, then gambling losses are deductions, no matter by what name they be called. As to 1942 and 1943, there is a 15% limitation on charity donations (which was not

exceeded in any event by any theory) and gambling losses are entirely deductible without limitation of percentage up to the amount of gambling winnings in the year. Where it is contended the defendant had substantial gambling winnings, it would not make any difference which it were called, charity or gambling losses, for it would be deductible items. Defense objection to the line of questioning calculated solely to appeal to the prejudices of those composing the jury, for calling a deduction allowable in any event by whatever name it might be called, was overruled by the Court. Tr. 828.

13. Upon cross-examination of the defendant as a witness, upon the issue of a substantial part of the inventory of liquor having become unmerchantable, and therefore to be written off in the accounting period it became unsalable, the prosecution listed the inventory, US Exhibit 34, giving the merchandise by name, brand and quantity, and questioned her. On re-direct examination, the defendant was asked as to certain brands in the inventory. She testified that the YPM whiskey had to be given away; it was on the premises and she didn't make up that report. Asked about Rico Rye, it was objected to as immaterial; and the court sustained the objection. Asked as to the brandy on the inventory, she said she could not sell it over the bar. The prosecution objected and the objection was sustained. Asked if she had any call for these cordials in the inventory, it was objected to and sustained. Tr. 840-1, and Suppl.

Merchandise that becomes unsalable is to be written off in the accounting period in which it becomes unsalable.

3 *CCH. Federal Tax Reporting Service* 609, Sec. 120 et seq.

14. Defense counsel assigned as error the prosecution counsel's interposing of objections to extract a prosecution witness from a difficult position. (Tr. 36.) The Court reprimanded defense counsel before the jury for assigning error. The objection of the prosecution was too obviously ill founded to justify its imposition, and the argument advanced in the objection bore no relation to the objection. Such conduct is a mere trick at best, and misconduct of counsel. When it becomes grounds to censure defense counsel for assigning as error conducts of the prosecution which defense counsel believes in good faith to be well founded, and which must be specified in the record, and leave an unfavorable impression in the jury's mind that defense counsel, not prosecution counsel, was acting improperly, then it becomes dangerous to protect an accused's record. This act of the Court could not but have had prejudicial effect upon the defense of the charges, and damaged the defense irreparably.

**The Written Judgment does not conform to the Judgment pronounced by the Court.**

The Court pronounced the judgment and sentence (Tr. 906):

“The Court: Well, it is the sentence of the Court and it is ordered by this Court that the defendant be committed to the custody of the Attor-

ney General or his authorized agent or representative, to be imprisoned for a period of six months and pay a fine of \$5,000. And at the end of that period of time, you will have plenty of time to look into the civil aspect and the criminal aspect as well, and determine whether or not we should go on with the other two counts under the indictment.”

The judgment entered in the record specifies not only the 6 months imprisonment and \$5,000 fine, but also the imprisonment of the defendant until the fine is paid.

The written judgment should conform to the judgment pronounced in court.

*Hill v. U.S.*, 298 US 460, 56 S. Ct. 760, 80 L. Ed. 1283.

**Numerous important instructions were requested by the Defendant but not given by the Court.**

The instructions requested and not given, are set forth at length in the appendix.

1. The defendant purchased the Baker St. apartment house for \$7,000 cash and the property was subject to a deed of trust for \$10,000 made by the vendor to another. The mortgagee insisted upon collecting and applying all the rents, as a condition of the sale. The defendant requested an instruction following *Hilpert v. Commissioner*, 5 Cir. 151 F. 2d. 929 that where the mortgagee under an assignment of rents, collects the rents and applies them upon an obligation under which the defendant has no legally enforceable liability upon the debt, such is not income to the taxpayer. This



was covered in Defendant's proposed instruction No. 1.

In line with this, Defendant's proposed instructions No. 2 and 3, setting forth the law of California, CCP 580b and *Stockton Sav. & Loan Bank v. Massanet*, 18 Cal. 2d. 200, 114 P2d. 592, that there is no personal liability for a purchase money mortgage, particularly one in existence and the land purchased subject to such a mortgage of another.

3. There was considerable testimony upon questioned writings and who wrote them. The federal statute, 28 USCA 638, was requested as Defendant's proposed instruction No. 4; it was agreed upon by the prosecution as a proper instruction. The Court did not give it, nor anything concerning the province of the jury in making comparisons.

4. There was some testimony offered by the government as to inventories, and some of the testimony of the agent Krause as to income using inventories. A "cash basis" was used by the taxpayer in making her returns, and she was entitled to an instruction as to the "cash basis". None was given. Proposed Instruction No. 5 was refused.

5. Defendant's proposed instruction No. 6 was not given. There was no instruction given stating that the prosecution had the burden of proof to prove taxable income, and gross receipts are but one item going to make up taxable income.

6. Defendant's proposed instruction No. 7 based upon *Hargrove v. US*, 67 Fed. 2d. 820 was not

given. There was testimony as to the belief of the defendant as to certain items not being taxable. An instruction should have been given that honest or bona fide belief of the defendant at the time of making her return involved in the indictment that certain income was not taxable, or mistaken concepts of law or of accounting or of taxation, negatives the specific intent required as an element of the offense. There was no instruction given covering this point and defense.

7. Defendant's proposed instruction No. 8, based upon *Hargrove v. US*, 67 F. 2d. 820, was requested, covering the rule that one is ordinarily presumed to know the law has no application in the offense charged; ignorance of the law is a defense, and the defendant must do the affirmative wrongful act charged knowing it was a violation of the specific law. The Court garbled this proposed instruction into one that the defendant could not be found guilty unless the jury found she knew that the law required her to file true and correct income tax returns! Specifically, the defendant did not know what was or was not taxable income, and was not informed until after the 1944 returns were filed that gambling income was taxable, although she deposited that income openly in her bank account, and it was from that source that the agents claim to have picked up the source of income.

Proposed Instruction No. 9, following the Hargrove Case that a person was not guilty of a felony within the provisions of Sec. 145b because the taxpayer had a mistaken concept of what was or was

not reportable income, or allowable deductions, or because of forgetfulness at the time of making the return, was not given.

8. Defendant's proposed instruction No. 10, covering the doctrine of *respondiat superior* not being applicable to criminal cases; and a principal is not responsible for the criminal acts of an agent unless there be command, direction or consent to the doing of the very act, was not given. This is clearly the law; and the defendant was sought to be convicted for the acts of her accountant, Bosserman, and for the acts of her husband in closing the register and giving her the totals which in many instances were items entered in the "black book".

*People v. Armentrout*, 118 Cal App. 761, 1 P 2d. 556.

*Paschen v. US*, 70 F 2d. 491.

*Noble v. US*, 3 Cir. 284 Fed. 253.

Defendant's proposed instruction 11 clarifies the above instruction as to the meaning of "*respondeat superior*", and applies the rule. It was not given.

9. Defendant's proposed instruction No. 12, based on *Cooper v. US*, 8 Cir. 9 Fed. 2d. 216 on clerical errors of employees, accountants, etc., in making the return not being a criminal responsibility of the defendant, was not given. Nor was 13, which combines the rule of the Hargrove case that the intent must be present to do an act knowing the law denounces it.

10. The various instructions proposed by the defendant based upon the *Spies v. US*, 317 US 492,

87 L. Ed. 418 were not given. Proposed Instruction No. 14, not given, was taken in substance from the Spies Case and the one which the Court held should have been given. Proposed Instruction No. 32 as to wilful failure to pay a tax was not given. Proposed Instruction No. 33, that an affirmative wilful attempt is not presumed but must be proved, and the burden being upon the prosecution, was not given. Proposed Instruction No. 34, which is virtually the language of the Spies Case decision, with a few omissions where it is not material, was also not given.

11. A number of instructions involving community property were requested. It was a material law in the case at bar, and materially involved the defense. A very limited instruction was given, which could not but have misled the jury. The facts are not denied, and indeed the prosecution's own case proved that the defendant was married in March, 1942, to Mr. Jost; lived with him until July, 1943, in California, when they separated and an interlocutory decree was entered in July, 1943, silent as to any property; and the final decree dissolving the community was not entered until the middle of 1944, also silent as to property. It would be impossible to determine the wife's income without reference to the law of California concerning husband and wife, and their respective interest in property acquired by either of them or by both during their marriage. It is interesting to note that the Indictment 1st count, charges the wife with *all* the earnings of her husband, Jost, earned by him



prior to their marriage in 1942 as well as all subsequent to their marriage—\$1380. So does the Krause computations and account, Ex. 28.

As is the usual practice in divorce cases, the wife claims everything she has in her name or possession at the time of filing the divorce as her separate property, relying upon the presumption in the code. Counsel for plaintiff wives in divorce actions know that often the husband will not contest, and default. Thus there is no problem for the court to award the property, as there is if it is alleged to be community property. If it is contested, the presumption of property in the name or possession of the wife, must be overcome by proof. This is just what the defendant did in her divorce action and the husband defaulted.

A proposed instruction, No. 56, following the decisions of *Brown v. Brown*, 170 Cal. 1, 147 P. 1168, and *Lorraine v. Lorraine*, 8 Cal. App. 2d. 687 48 P. 2d. 48, was proposed, and not given. If the wife claimed the property as separate in the divorce complaint, there was a default, it was a contract between the parties, that all community property pass to the plaintiff wife as her sole and separate property.

Proposed Instruction No. 16, that property or money acquired from the community upon a separation, is not income to the wife, whether by agreement or judgment, was not given.

Proposed Instruction No. 18 set forth *California Civil Code Section 172*, as to the management and

control of community property, using the words of the statute. It was not given.

Proposed Instruction No. 19, that earnings of a wife while living with her husband are community property, was not given.

Proposed Instruction No. 20, that earnings of the defendant while living with her husband are community property under his control the same as other community property, was not given.

Proposed Instruction No. 21, following *Lawrence Oliver v. Comm'r*, 4 Tax Court 684, and *Periera v. Periera*, 156 Cal. 1, 103 P. 488, as to the allocation of earnings in a business which originated as the separate property of one spouse, and a principal part of the income is attributed to the personal services of one or both spouses, which is community property, was not given. This is the very thing presented in the three years involved. The defendant had a half interest in the Bar, representing a \$1000 investment at the start of 1942. She was married in March, 1942, to Mr. Jost. Upon the credit of the community, and earnings of the community saved as of July 16, 1942, the other half interest in the bar was acquired for \$1650. The principal income was from the services of the wife and the husband while living together in California for the time in issue in 1942 both from the partnership and when the partnership with Divers was ended.

Proposed Instruction No. 22, following *Roches v. Blair*, 9 Cir. 32 F. 2d 22 that commingled community and separate property so as not to permit the identity of the portion that is community and

the portion that is separate, all is presumed community, was requested and refused. This is the fact in all three years. Surely the income during the time the parties lived together until July, '43, and after their separation was not determined, nor was there any attempt to segregate how much of the bar business acquired after the marriage in March, 1942, nor the increase in its assets as the liquor in the inventory, etc., were community or separate. It was not until late July, 1943, that the interlocutory decree was entered, and not until a year after that in 1944 that the community was dissolved, and the divorce dissolved the community and became effective as a contract between the parties that providing all was solely separate property of the wife.

Proposed Instruction No. 24, that property acquired upon the credit of the community is community property, was not given. In the case at bar, the government's evidence was that borrowed money was used to acquire the second half interest in the bar in July, 1942, for \$1650.

12. There was testimony that the defendant acquired some money from gambling in wholly friendly games with competitors. Proposed Instruction No. 26 stated that income from unlawful business is taxable, money obtained in a game of chance undertaken solely for amusement and not as a business is not taxable income. An alternative proposed instruction No. 25 was proposed adding the additional element that the gambling must be not prohibited by law. Neither was given.

Property received by chance, not connected with a business venture, is not taxable.

*McDermott v. Commissioner*, 150 F. 2d. 585.

*Washburn v. Commissioner*, 5 Tax Court No. 162.

13. There was much testimony on expenses incurred by the defendant in business entertainment to enhance her bar business. Proposed Instruction No. 27, that it was a deductible expense in arriving at taxable income, was not given.

14. There was testimony that the sister of the defendant worked for her, and received living quarters and accommodations. Proposed Instruction No. 28, that this was an expense to be deducted from gross income in arriving at taxable income, was not given.

15. There was testimony that the automobile was used part for pleasure and part for business, and proposed Instruction No. 29, as to pro-rating of such expense, was not given. The living accommodations shared with the sister is within the same rule.

16. Instruction No. 30, on depreciation and the rate, was not given.

17. Instruction 31 as to employing an accountant was given, but injecting the word "truthful" before the word "book". In view of the prosecution's misconduct in making such an issue of entries of donations in place of gambling losses, which was over a thousand dollars in 1944, notwithstanding the defendant taking a standard deduction where the amounts for charities bears no relation to the



tax; and the amounts were small in 1942 and 1943, and were a deduction in any event; this instruction was most misleading, and erroneous. The error in the books must be as to a matter that would have a direct and proximate connection with the ultimate tax, for it to defeat the defense. In addition it must be such an error that was made with a present knowledge that the error in the books was calculated to defeat and evade the income tax, and with that intent. The instruction as proposed included the element of "relied in good faith upon the tax return" which would negative any such intent. As drawn, the instruction was proper. As given, it was very misleading and erroneous.

18. Proposed Instruction No. 35, on "willful" as defined in *US v. Murdock*, 290 US 389, 54 S. Ct. 223, L. Ed. 381 was not given, but instead an instruction including negligence, that is careless as to the requirement of the law, was given. In tax law, there is a strong difference between "fraud" and "negligence", and the subject of a number of decisions. Suffice it to state that *negligence* is not proof of the "willful" intent under the felony charge of Sec. 145b. This error of the court in the instructions is most damaging to the defendant.

19. Defendant's proposed instruction drawn from *Hargrove v. US*, 67 F. 2d. 820 on "willful and knowing" as used in describing the offense, was not given. The essence of the law is not the doing of a certain act knowing that the act is done, but the specific wrongful intent that is the actual knowledge of the existence of the obligation im-

posed to return a specific money as income, or not to take certain deductions that are the offense. Every taxpayer who files a return does the act “willful and knowingly”. It is only those acts done “willfully and knowingly” with an attempt to evade the income, as knowingly misstating income, knowing the correct income, knowing the requirement of law, but who keeps two sets of books, one correct and one for the income tax as a lesser sum, who meets the test of “willful and knowingly” under the statute making it a felony. A taxpayer who keeps daily cash register total for sales tax matters, who deposits all income in bank accounts openly, and then gives the cash register daily totals and the bank account records to an accountant to compute the income tax, is not within the language of “willful and knowing” of the statute, though the return relied on in good faith, prepared by the accountant, is filed with the positive knowledge and positive acts of the taxpayer.

20. Defendant’s Proposed Instruction No. 38, based on the *Hargrove Case* requiring every element of the offense to be proved as done with actual knowledge of a specific violation of the income tax law, was not given.

21. Defendant’s Proposed Instruction No. 39, requiring a specific intent to defraud be proved, and Proposed Instruction 40 defining fraud, were refused.

22. Defendant’s Proposed Instruction No. 42, as to discovery of omission after the return, was refused. There was evidence that after the 1944

return was filed, Bosserman told the defendant to keep records of gambling winnings and losses, and she was surprised to learn it was taxable; but no proper instruction upon this, and the jury might well conclude that she had a duty immediately upon the discovery and not to wait until she appeared with her counsel at the Intelligence Unit to offer to file another return.

23. Defendant's Proposed Instruction No. 43, that a tax liability must exist to attempt to evade it, and the duty was upon the prosecution to prove the tax as an element, was not given. Neither was Proposed Instruction No. 44 that this burden of proof never shifted and the quantum of proof and presumption in criminal matters as to a tax is not the same as in civil cases where the Commissioner makes a determination and it is *prima facie* correct.

24. Proposed Instruction No. 45, that a taxpayer does not act at his peril of prosecution under Sec. 145b when he returns and reports income which he or she may believe proper, was not given. Neither was proposed Instruction No. 46, that if a taxpayer entertains a doubt as to what is or is not reportable or deductible expense, he is free to resolve all doubts in his or her favor; that regulations are not always in accord with judicial decisions, and it is not the intent of Congress under Sec. 145b to punish such acts as a felony.

It might be pointed out that there are numerous times that a taxpayer or his advisor holds doubts as to the legality of a regulation of the Commissioner. The practice is to construe the doubts

favorable to the taxpayer in the return, expecting to take the matter up if raised by the Commissioner on administrative procedure, then to the Tax Court, rather than to pay every possible sum and sue for recovery in the District Court.

25. Proposed Instruction No. 47, covering losses from transactions for profit, not in the trade or business, are deductible, was not given. The defendant suffered fire losses, etc., from her rented flat in 1942 and other losses not connected with the bar.

26. Proposed Instruction No. 48, as to the deductibility of bad debts, was not given. There was evidence that the defendant suffered losses from loans and bad debts in the year 1942 as well as other years. Instruction proposed as No. 49, permitting a reserve for bad debts at the option of the taxpayer, was also not given.

27. There was the question as to whether in the year 1942 in which she and her husband were married in March and lived together in California, filed a joint return, she was criminally responsible for reporting his income under the community property law (over which the law gave him absolute control and disposition), or whether she was merely criminally responsible for her own income, as well as the husband's wages before the marriage. An Instruction No. 51 proposed, following *Cole v. Commissioner*, 9 Cir. 81 F. 2d. 485, was not given.

As the law was enunciated by the Court, the wife having neither control or disposition of community property by law, is criminally responsible



as a felon for failure to return income of the community and her husband need only be divorced from her to be a prosecution witness and avoid his just desserts. How concepts of crimes do vary!

28. The *Current Tax Payment Act of 1943* was covered in Proposed Instructions No. 52 and 53. Not only did the Court refuse it, but on the contrary instructed the jury that the Federal statute did not apply! The last sentence of the Act, Section 6a, reads:

“This subsection shall not apply in any case in which the taxpayer is convicted of any criminal offense with respect to the tax for the taxable year 1942 or in which additional tax for such taxable year are applicable by reason of fraud.”

Obviously, the provisions as to conviction could have no application during the trial, and the Court cannot assume the defendant convicted before or while it instructs the jury, for that is pre-determining the case and throwing out the presumption of innocence that is inherent in our jurisprudence. There has been no assessment of any tax, nor for fraud. The Court excluded any evidence that there was no assessment, although if there had been an assessment for 1942 for fraud, it is at least arguable that the Act would not apply. Furthermore, the prosecution contended that there should be no instructions on fraud, as it was contended this action was not sounding in fraud; the prosecution cannot then contend that the instant matter is fraud when this section is asked as an instruction. Certainly, the Court cannot give its instructions in a

criminal case assuming the accused is guilty of fraud for the year in which she stands charged with attempted wilful evasion, merely from the indictment.

This is the so-called “Forgiveness Act” which imposed the duty upon the prosecution witness Jost to report and pay the 1942 tax as part of 1943, and which we must assume he did, for he was married during March, 1942, and lived with the defendant to July, 1943, and the marriage was not dissolved until the final decree in 1944. The prosecution offered him as a witness, objected to all inquiry as to his income tax returns for 1943. The prosecution sought to convict the wife based on community income, under the husband’s absolute control and disposition as a matter of law, for a tax forgiven and which the husband, vouched for by the prosecution’s production of him as a witness, should have paid and reported in his 1943 return, and we must assume he did.

29. The testimony of both the prosecution and defense showed that the alleged acts for which the indictment was brought and which the prosecution sought to charge as an offense were done by the wife in the presence of her husband; the books were kept during July, August and September, 1942, by the parties working together at the bar business, and the return was signed in their joint presence; they both lived over the bar in the same structure during all of this time. Defendant requested instructions No. 57, 58, 59 and 60 on the applicable law that a wife is presumed to act at

the coercion of her husband. The prosecution called the former husband Jost, and evidently assumed it could not disprove the coercion, for no effort on direct evidence was made to go into it. The defense could not cross-examine in a field not covered by direct examination. The defense did prove that Jost instructed the defendant to open a new book on July 16, 1942, when Diver's interest was bought out; and that some evenings Jost closed the cash register, brought the money and cash register totals to the defendant and she entered them in the "black" book as he gave them to her.

30. Individual directed verdicts for the defendant on each count were requested and refused.

The Court undertook to instruct the jury on all the complicated income tax law applicable in a few short instructions. We find no fault with the brevity, but we do by the omissions of the material issues left completely uncovered by instructions. The Court instructed that earnings of the defendant while living apart from her husband were separate property, leaving open and to inference to the jury that living together it might also be separate property.

The Court gave a formula instruction amounting to a direction to the jury to disregard community property. Purchase of a half interest on the credit of the community is of necessity community property, but the Court erred in stating it was separate. The Court omitted any of the evidence of the prosecution and the defense that Jost invested his salary in the business when he worked

and lived together, in the formula instruction. The Court assumed that and in the formula instruction stated that the proof was that Jost made no claim to community property, when Jost testified at the time of the interlocutory decree he consulted a lawyer, verified a pleading for his lawyer that he claimed community property in the bar, in a proceedings to set aside the default. The formula instruction stated that defendant stated under oath that there was no community property, which was not the evidence. She filed a verified complaint in divorce claiming all she had in her name or possession *at the time of the action* as community property, not that there never was community income.

The Court instructed that a relinquishment of Jost to community property claim was income. This is serious error for relinquishment is a gift, and gifts are not taxable as income. Neither are transfers of community to separate property by agreement or divorce decree taxable income.

The Court instructed that concealment of true income was an element of the offense. Concealment for other purposes than evading income tax are not punishable under Section 145(b) as a felony, and the instruction as given is highly prejudicial.

The Court instructed that any act, of whatever kind, which tends to evade income tax is enough to make up the crime! Far from it. The decisions are uniform that such is not the law, and there must be an affirmative wilful act done with a positive intent to evade income tax, with knowledge that it is evading the tax, as well as a tax owing



to evade to constitute the crime. This instruction alone is enough to reverse the judgment. The Court goes on to say that filing of a false return is an act that is an evasion and enough to make up the crime. This left the jury to determine if there was any mistake in the return, the defendant should be convicted! This is highly prejudicial error. This left the jury to determine if the return differed from the testimony of the agents as to any matter, it was enough to convict! This is highly prejudicial error.

The Court instructed as to “willful” in the alternative, not in the conjunctive as set forth in the Spies and Murdock cases. The Court instructed that *careless* disregard as to whether one has the right to do the act was of itself “willful” within the statute! *Negligence or carelessness* as to law as to how one shall make an income tax return is not a felony, and Congress never intended it to be. Yet the Court instructed the jury it was and no doubt the jury considered the defendant might have been negligent in seeking to discover the law as to what was or was not taxable or was or was not deductions, and returned their verdict accordingly. This is error of the grossest kind.

The Court instructed the jury that “willfulness” could be inferred or presumed, rather than requiring the prosecution to prove by evidence beyond a reasonable doubt and to a moral certainty each element including the essential element of “willfulness” made the subject of the Spies and Murdock

cases as an essential distinction between the misdemeanor and the felony.

The Court instructed the jury that the prosecution had proved she was the sole proprietor of Kay's Club, she knew the true amounts of her gross income! As if the defense of forgetfulness had no application. As if she were charged criminally with knowledge or acts of her agents, servants, or accountants she did not direct but which took place within the scope of their employment. As if the doctrine of respondeat superior applied to criminal cases! As if a person could actually remember every detailed transaction during an entire year, no matter how inconsequential and no matter by what servant, agent or accountant it was conducted! This instruction alone is per se, error and grounds for reversal.

The Court's instruction on material variance and that the government need only prove a "substantial" amount of tax was highly prejudicial. To some, \$10 tax is a substantial sum, to others \$172 is a substantial sum to earn in 6 months of business operations, but judged by the amounts charged in the indictment, and the various importance individuals in the jury attach to small sums, and the subjective standards to be attached to the word "substantial amount of tax", this was likely to mislead the jury, and should have contained the elements of material variance known to the law.

The Court instructed the jury that deposits in the bank account of the defendant were potent proof that such deposits were income, totally dis-

regarding the prosecution's testimony by their own agent that some bank deposits were proceeds of loans, and in total disregard of the custom of bars to cash checks, as shown in the evidence some were bad. Certainly, such an instruction in view of the testimony that some were checks cashed and deposited for collection, is error.

The Court instructed the jury that proof of money spent in a certain year was proof of income of the defendant for that year. In view of the proof of the husband's earnings going into the business, she should not be charged with more than her half under the community property law, *after* the marriage and not for the whole year. Money clearly borrowed by government testimony, and spent makes this instruction particularly vicious. Furthermore, the government's own evidence shows that for 1943 and 1944, the business ventures of rental property were a loss. Certainly payment of those losses are improperly instructed by the Court to be income—they are deductions in any theory, yet they were spent. Also money spent, representing liquidated assets by depreciation, is not income under any theory.

The Court instructed the jury that where there are joint returns of husband and wife, and a deficiency is asserted against one of the spouses for additional income, the spouse against whom it is asserted is liable. This is far from the law of the *Cole case*, and the mere assertion of a claim of tax never did incur liability, particularly in a criminal case where it must be proved. No doubt

the jury following this instruction took the bare assertion as raising the liability.

The Court by formula instruction, Transcript 887, instructed the jury that mere willful attempt to evade, was grounds to convict, even without any tax being due; and that the forgiveness feature did not apply where there was no fraud, assuming the defendant guilty of fraud!

A reading of the instructions, assuming that the jury knew no income tax law, nor law applicable to felonious wilful evasion of income tax, would certainly mislead a jury, and leave many issues without instructions. If we assume the jury knew what the ordinary layman knows of tax law, the points uninstructed would leave a kaleidoscope of divergent views, many erroneous, involving many material issues. This is not the essence of a fair trial, for the accused is entitled to be tried upon instructions that fairly state the law involved, upon the issues presented.

### CONCLUSIONS

1. The Bill of Particulars was improperly denied, resulting in surprise and injury to the defense.

2. There was no case made against the defendant sufficient to uphold the verdict or judgment.

3. There are numerous errors in the record, that result in prejudice and damage to the defense.

4. The instructions did not properly state the law.

HOWARD B. CRITTENDEN, JR.,  
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*Attorneys for Appellant*



No. 11911

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United States  
Court of Appeals  
for the Ninth Circuit

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CATHERINE O'CONNOR,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

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Transcript of Record  
SUPPLEMENT

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Appeal from the District Court of the United States  
for the Northern District of California,  
Northern Division

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# INDEX

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

	PAGE
Affidavit of Howard B. Crittenden, Jr., in Support of Motion for Bill of Particulars.....	7
Affidavit of Catherine O'Connor in Support of Demand for Bill of Particulars .....	12
Court's Charge to the Jury.....	120
Indictment .....	2
Instructions Proposed by Defendant.....	94
Motion for Bill of Particulars or in Alternative to Make Indictment More Certain.....	5
Witnesses:	
Beal, Alberta .....	79
Bosserman .....	17, 28
Jost .....	24
Krause .....	42, 52
O'Connor, Mrs. ....	84
Shannon .....	26
Tormey .....	54, 72, 75, 82
Washland .....	1





\* \* \* \* —Washland—(Tr. page 36)

Q. Actually, your testimony at the prior hearing was that all discussion of gambling during these conferences covered the year 1945, wasn't it, and now your testimony is the conversations covered all those years, 1942, 1943, 1944 and 1945?

Mr. Campbell: Just a minute. That is objected to on two grounds: first, it is argumentative, and secondly, it does not state the record. The record indicates that the witness stated that she was asked to produce the returns for a number of years. She was asked general questions as to her sources of income. She stated in those years she was gambling. On cross-examination counsel has pulled out a question, saying, "You asked her a question as to gambling applying to 1945?" He said, "Yes, it did," which is not inconsistent with his statement as to what the general nature of the examination was. I suggest that his question is argumentative and it is not within the record on which he seeks now to impeach him.

Mr. Crittenden: May I assign as error the argument of counsel which is attempting to get his witness out of a difficult position?

Mr. Campbell: I object to that, if the Court please.

The Court: That statement is unwarranted. Let it go out and let the jury disregard it for any purpose in this case. I will sustain the objection on the ground it is argumentative. You will now proceed.

\* \* \* \*

The grand jury charges:

That on or about the 15th day of March, 1943, in the Northern District of California, and within the jurisdiction of this Court, Catherine O'Connor, also known as Catherine N. Jost and Catherine N. Larson, late of San Francisco, who during the calendar year 1942 was married and had no dependants, did wilfully and knowingly attempt to defeat and evade a large part of the income tax due and owing by her to the United States of America for the calendar year 1942 by filing and causing to be filed with the Collector of Internal Revenue for the First Internal Revenue Collection District of California, at San Francisco, a false and fraudulent joint income tax return wherein she stated that her net income for said calendar year was the sum of \$777.29 and that no income tax was due and owing thereon, whereas, as she then and there well knew, her net income for the said calendar year computed on the basis of a joint return was the sum of \$6,359.47, derived as follows:

*Gross Income*

Net profit from bar .....	\$2,785.92
Salaries .....	1,380.00
Rental Income .....	303.00
Partnership Income .....	2,116.05
Total.....	\$6,584.97

*Deductions*

Contributions .....	\$152.50	
Interest Paid .....	73.00	225.50
Net Income.....		\$6,359.47

upon which said net income she owed to the United States of America an income tax of \$1,103.46 (26

U.S.C., 145(b); Section 145(b), Internal Revenue Code).

## SECOND COUNT

The grand jury further charges:

That on or about the 15th day of March, 1944, in the Northern District of California, and within the jurisdiction of this Court, Catherine O'Connor, also known as Catherine N. Jost and Catherine N. Larson, late of San Francisco, who during the calendar year 1943 was married for six months and head of a family for six months, did wilfully and knowingly attempt to defeat and evade a large part of the income and victory tax due and owing by her to the United States of America for the calendar year 1943 by filing and causing to be filed with the Collector of Internal Revenue for the First Internal Revenue Collection District of California, at San Francisco, a false and fraudulent income and victory tax return wherein she stated that her net income for said calendar year was the sum of \$7,879.28 and that the amount of income and victory tax due and owing thereon was the sum of \$1,707.75, whereas, as she then and there well knew, her net income for the said calendar year was the sum of \$21,608.91, derived as follows:

### Gross Income

Net Profit from bar .....	\$ 21,694.25
Rental Income .....	324.66
Total.....	\$ 22,018.91

### Deductions

Contributions .....	\$255.00	
Taxes .....	155.00	410.00
Net Income .....	\$ 21,608.91	

upon which said net income she owed to the United States of America an income and victory tax of \$8,038.65. (26 U.S.C., 145(b); Section 145(b), Internal Revenue Code.)

### THIRD COUNT

The grand jury further charges:

That on or about the 15th day of March, 1945, in the Northern District of California, and within the jurisdiction of this Court, Catherine O'Connor, also known as Catherine N. Jost and Catherine N. Larson, late of San Francisco, who during the calendar year 1944 was single, did wilfully and knowingly attempt to defeat and evade a large part of the income tax due and owing by her to the United States of America for the calendar year 1944 by filing and causing to be filed with the Collector of Internal Revenue for the First Internal Revenue Collection District of California, at San Francisco, a false and fraudulent income tax return wherein she stated that her net income for said calendar year was the sum of \$5,091.98 and that the amount of tax due and owing thereon was the sum of \$1,131.67, whereas, as she then and there well knew, her net income for the said calendar year was the sum of \$24,530.88, derived as follows:

<i>Gross Income</i>	
Net profit from bar .....	\$ 24,579.05
Rental Income .....	451.83
	<hr/>
Total.....	\$ 25,030.88
<i>Deductions</i>	
Standard Deduction .....	500.00
	<hr/>
Net Income.....	\$ 24,530.88



upon which said net income she owed to the United States of America an income tax of \$10,299.15 (26 U.S.C., 145(b); Section 145(b), Internal Revenue Code.)

A True Bill:

.....,

Foreman.

.....,

United States Attorney.

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MOTION FOR BILL OF PARTICULARS OR  
IN ALTERNATIVE TO MAKE INDICT-  
MENT MORE CERTAIN

To the Above Entitled Honorable Court:

The defendant Catherine O'Connor having made a demand for a bill of particulars, and a response having been made by the plaintiff attaching photo-static copies of the tax returns requested, and having specified that defendant's husband earned the salary sought to be charged to defendant in 1942 by the indictment in the above-entitled matter; and the Penal Division, Treasury Department having advised defendant's counsel that the "cash" method of accounting and not some other method involving inventories having been used, but having refused to provide the items of gross income and sources or the items of expenses and deductions to make up the item of "net income from bar" set forth in the indictment in each of the counts for each of the years 1942, 1943, and 1944;

The defendant Catherine O'Connor moves for a further bill of particulars to set forth said items requested and refused in her demand for a bill of particulars; and reference is hereby made to her demand filed in the above-entitled matter.

And in the alternative, if such bill of particulars be denied or refused for any reason, said defendant moves that said indictment be made more particular by the setting forth of the various items of gross income giving the various sources, and the items of expense and deduction (showing each item) upon which the "net income from bar" is alleged in each count, for the years 1942 in first count, 1943 in the second count, and 1944 in the third count of said indictment.

Said motion is made upon the indictment, the Demand for Bill of Particulars, the Response filed thereto by the Plaintiff, affidavit of the Defendant for Bill of Particulars, and affidavit of counsel for Defendant for Bill of Particulars, and upon the records and papers on file in the above-entitled matter.

/s/ HYMAN & HYMAN,

/s/ HOWARD B. CRITTENDEN, JR.,

Attorneys for Defendant.

**AFFIDAVIT IN SUPPORT OF MOTION FOR  
BILL OF PARTICULARS**

State of California,

City and County of San Francisco—ss.

Howard B. Crittenden, Jr., being first duly sworn, deposes and says: that he is one of the attorneys for the defendant in the above-entitled matter. That the attorneys for the defendant have held an informal discussion with Mr. Walter Campbell, Chief of the Penal Division of the Treasury Department, Mr. Siegel, and attorney in said division, and with auditors and agents of the Bureau of Internal Revenue relative to the figures involved in the indictment in the above-entitled matter. That a bill of particulars has been delivered providing copies of the returns, stating that the wages were those of the defendant's husband in 1942, and it was stated in said informal conference that the cash method of accounting and not the hybrid or any other system using inventories were used in arriving at the alleged amounts set forth in the indictment.

That in the course of said discussion it appeared that the defendant kept and maintained together with other records, a grey book covering the financial transactions of the partnership in which the defendant was a partner, in addition to books and records of the defendant's personal transactions. That said grey book contains the only records of the said partnership; and said partnership had income which the first count of the indictment al-

leges there was income chargeable to the defendant. That said partnership book of account in said grey book is in the possession of said Penal Division of the Treasury Department, Bureau of Internal Revenue, and not in the possession of the defendant. That said book contains the only records of the defendant covering the partnership financial transactions during portions of the year 1942.

That in the course of the said discussion it appeared from statements made by said Chief of the Penal Division, and from statements of the agent of said Treasury Department at said discussion, that there exists during the years 1942, 1943 and 1944, and each of them, financial transactions of the defendant which are allowable deductions of the defendant for income tax purposes, which said financial transactions did not appear in any of the records of the defendant. That placing his information upon said statements, and upon his discussions and interrogations of his client, affiant believes and therefore alleges that there are items, transactions, and expenses of the defendant which do not appear in her books or records, and which by reason of the passage of time are no longer within the knowledge or present recollection of defendant, and which items, transactions or expenses either were handled by agents or servants of the defendant or which the defendant has forgotten. That said items, transactions, and expenses are necessary for the defendant to properly prepare her defense in the above-entitled matter, and can be obtained only by a bill of particulars.



That in one of said informal discussions, it was stated by the said Mr. Campbell and by agents of the United States Treasury present at such discussion, that affiant's books did not include or show various income of the defendant during the years of 1942, 1943 and 1944. That affiant placing his information upon said statements, upon his examination of the books, records, and papers of defendant, and upon his conference with his said client and his interrogation of his client believes and therefore alleges that there are sums of money in each of said years, properly includable as gross income for income tax purposes, not shown by said books and not within the knowledge or present recollections of his client; that affiant does not have information or belief as to the items or extent of said income sufficient to prepare a defense in the above-entitled matter, and the only remedy is to obtain a further bill of particulars.

That in the course of said discussion, it appeared that there was several thousand dollars of difference between the government's alleged figures for the year of 1943 and the defendant's books and records. That by reason of this variance in both the alleged income and the variance in the amount of deductions allowed or allowable or known, it is impossible for defendant and defendant's counsel to prepare a defense to the alleged matter set forth in the indictment.

That the defendant was involved in numerous, complicated and extensive financial transactions during the years 1942, 1943 and 1944, and in 1942

a portion of the year in a partnership with another. That part of said financial transactions are material and part are not material in the issues and proper trial of the above-entitled matter. That unless the items making up the gross income and the items making up the business expenses and deductions are set forth in a bill of particulars, with particularity, the defendant will be unable to properly prepare a defense, know the nature and character of the charges against her, cross-examine witnesses; and a great number of irrelevant figures and computations will be gone into at the trial which cannot but prejudice a jury against the defendant, unduly complicate the issues, confuse the issues, and seriously prejudice the defendant.

That the affiant has used various methods of attempting to arrive at the alleged taxable net income or tax liability attempted to the alleged in the indictment, and in doing so affiant has used all the books, records, papers and information supplied him by his client; and affiant has used the "cash in cash out" system, a "net cash" system, a computation using an extension of cost of merchandise using an approximate markup, a "net worth" system, and a totalling of all money shown to be disbursed by accounting periods. That the personal accountant for defendant, Maurice Hyman and affiant spent the better part of one day attempting to use the various systems to estimate or approximate or to arrive at any basis for the figures alleged by the plaintiff. That all of said methods produced estimates approximating more

closely the figures reported by the defendant as her income subject to tax than the figures alleged by the government as taxable net income or income from business. That affiant is at a loss to know or upon which alleged facts, if any, the plaintiff seeks to arrive at the figures alleged in the indictment as "net profit from bar", or which the gross is alleged to have consisted of, or from which or what source it is claimed, or what deductions or expenses were allowed in arriving at such "net profit from bar".

That affiant is informed by the government officials at said discussion, and believes and therefore alleges that the Treasury Department Agents have arrived at said figures of "net profit from bar" in each of said years 1942, 1943, and 1944 upon figures not wholly obtained from the books or records of defendant, but upon facts which are outside of the knowledge of defendant, or within her personal present recollection, and which were obtained by investigation of records and sources available only to an agent or official of the Bureau of Internal Revenue through its powers in investigation of tax matters; and such records, statements, and evidence are not within the reach, authority or inquiry of the defendant or her counsel for want of said means and access of records, statements and evidence granted such government officials, of third parties.

That it is affiant's opinion as counsel for said defendant, that said defendant cannot safely proceed to trial without the items of the bill of par-

ticulars refused to be supplied by plaintiff, and which affiant must have to properly prepare a defense for his client in the above-entitled matter, to cross-examine witnesses offered by the plaintiff, and for the Court to determine the materiality and relevancy of the tremendous amount of testimony covering the numerous financial transactions that would otherwise be injected into the issues upon a trial.

/s/ HOWARD B. CRITTENDEN, JR.,

Subscribed and sworn to before me this 25th day of August, 1947.

(Seal) E. J. CASEY,

Notary Public in and for the City and County of San Francisco, State of California.

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AFFIDAVIT OF CATHERINE O'CONNOR IN  
SUPPORT OF DEMAND FOR BILL  
OF PARTICULARS

State of California,

City and County of San Francisco—ss.

Catherine O'Conner, being first duly sworn, deposes and says:

That she is the defendant in the above-entitled proceedings indicted under 26 USCA 145b for the returns she filed for taxable years 1942, 1943, and 1944. That in each count of the indictment it is stated that she received "Gross Income" itemized as various items of net income. That her financial



records and books of account, vouchers and bank statements of those years are such that they approximately support her original returns but there is a great differential between the sums alleged in each year of the indictment as between "net income from bar" and "rental income". That her accountant and the person drafting various tax returns of hers, Mr. Bosserman, have held lengthy conferences with affiant's counsel in the above-entitled matter, and affiant is informed by them and believes and therefore alleges that there appears to be no correlation between the amounts alleged as such items of "net income from bar" and "rental income" in the indictment counts and her records and books of her financial transactions for each of the years covered in said indictments; nor can it be ascertained what sum or sums are sought to be charged as gross receipts or from what sources, which sums of deductions, expenses and costs of business have been allowed or disallowed or in what sum.

That it is necessary for affiant to prepare her defense to the indictment in the above-entitled matter; and it is impossible to do so without advising her said counsel of the facts or the matters charged; and that she does not know and cannot ascertain in what manner or for what amounts and from what sources the indictment seeks to predicate the gross receipts, or how much thereof is from sales of drinks, sales of liquor, music box receipts and other rentals, the items deducted therefrom to arrive at "net income from bar" such as the items of rent, salaries, wages, stock purchases, depreciation of equipment (or the base, period, or

amounts allowed in that figure) or the items of rent sought to be charged to affiant, the depreciation schedules including base, rate, etc., and what items of deduction were allowed or disallowed as taxes, repairs, maintenance, insurance, etc. That she is unable to ascertain what methods or periods of accounting were used in the determinations alleged in the indictment, or the computations to arrive at the sums alleged.

That ordinary tax practice before the Internal Revenue Department involves an assessment with statements of items of deduction disallowed, and items of income sought to be charged, and the reasons therefor. That affiant has not the benefit of any such assessment or a statement of the grounds or computation thereof. That it is necessary that it appear in the bill of particulars by items, for example, some sum for wages for a certain year may appear to be allowed as a deduction, when in fact affiant may well have paid a greater sum. Upon the trial it will be necessary for each employee's wages for each month to be proved, unless the bill of particulars states with certainty which employee's salaries or compensation are allowed and for what sum, as allowable deduction or it appears which employee's wages are disallowed. That the three years covered by the indictment involves a great mass of financial transactions by and on behalf of affiant; and from the indictment she cannot advise her counsel which items are questioned or made the basis of the said three counts, and the public offense therein sought to be stated, or which items were allowable

deductions or which items were disallowed to arrive at the alleged sums, or what income is sought to be charged to affiant in any particular accounting period, or whether actual or constructive receipt is the theory for setting forth such receipt of moneys.

That without the bill of particulars requested in the above-entitled matter, it will be impossible for affiant to advise her said counsel of the factual matter involved in her alleged offense or in her defense, nor will it be possible to prepare a defense nor will it be possible for her counsel to properly cross-examine witnesses brought forth by the prosecution, nor to be able to rebut or test the testimony sought to be produced, nor for the Court to determine the materiality of evidence sought to be introduced. That without such bill of particulars, it will be impossible to conduct a fair or speedy trial of the issues nor to determine the material issues nor to present a clear and adequate defense to said charges. That without such bill of particulars it will be necessary to make judicial proof of every one of the numerous financial transactions made by or on behalf of affiant over a period of three years, 1942 to 1944 inclusive, and it will unduly take the time of the Court, counsel and affiant in such a proceeding.

CATHERINE O'CONNOR.

Subscribed and sworn to before me this 31st day of July, 1947.

(Seal)

THOMAS J. O'CONNOR,

Notary Public in and for the City and County of  
San Francisco, State of California.

\* \* \* \* (Tr. page 80)

Mr. Campbell: At this time we are going to offer in evidence Government's Exhibit 14, the ledger which has previously been marked for identification with the same number.

Mr. Crittenden: We will object to anything in the record after the 16th day of July 1942 going into the record as writing not proved, not shown to have been made by the defendant, not shown to have been made in the regular course of business, or that it was a proper or an original entry made by anybody at her instance or request or under her direction, or that it was made by any person who made it—in fact, they haven't even proved who made the entries after the 16th day of July, that the person making them had personal knowledge of the transaction or obtained such knowledge from a report regularly made to him or by some other person employed in the business whose duty it [80] was to make that report in the regular course of business.

The Court: Your objection goes to the foundation that has been laid for the introduction of this book.

Mr. Crittenden: After the 16th day of July 1942. Prior to that date we will stipulate that it was the partnership record, but after that date that is a disputed writing and has no place in the evidence.

The Court: Beginning on July 16?

Mr. Crittenden: That is right.

The Court: What is the answer to that, counsel?



Mr. Campbell: I will lay a further foundation, your Honor.

The Court: Very well.

Mr. Campbell: Q. What did the defendant state as to any entries made after July 15, 1946?

Mr. Crittenden: We have that affidavit here and I am going to object to that question. He has testified those were the statements that were made.

The Court: You may answer.

A. She stated that the entries made after July 15, 1942—

Mr. Campbell: Q. Yes.

A. In the receipts column were not made by her and that she did not know who made them. She could not give any explanation whatsoever for them.

Q. Now, as to the other entries appearing after that date?

A. As to the entries in columns other than receipts, in the paid-out column, she did identify certain other figures after July 16, 1942 as being hers and some of them as being those of her husband at that time, Mr. Jost.

Q. Did she identify any particular ones which you now recall and on what dates?

A. No, I can't recall the particular ones.

Q. Did she designate which ones?

A. She merely pointed them out, yes.

Q. You made no record of that at the time?

A. No, I did not.

Q. I call your attention further to certain obliterations appearing on the page for August, ink

obliterations appearing there over certain figures. Did you observe those obliterations at that time?

A. Yes, I did. As a matter of fact, the obliterations were much more complete originally in this book.

Q. Will you explain that?

A. In order to find out what was underneath all this scratching out, I took a soft eraser and to the best of my ability removed the top scratchings, which were in pencil. Originally it was so covered you couldn't read any of the figures under here, but I did remove by the use of a soft eraser most of the pencil.

Q. There were pencil obliterations on top of the ink obliterations that appear there?

A. Well, I don't know which was first, the pencil obliterations or the ink, but I was able to remove most of the pencil obliterations so I was able to read the figures.

Q. In connection with your examination of any of the books and records of Mrs. O'Connor's, did you observe some more obliterations in appearance to those on any of the records submitted by her?

Mr. Crittenden: We are going to object to any question as to what any other documents were unless they are produced. They are the best evidence of what they contain.

Mr. Campbell: I am asking the preliminary question, if I may first, your Honor. I am laying the foundation with respect to any other documents. I am asking him if he saw any. Then I will ask him what they are and then we will attempt to explain their presence or absence.

Q. Did you observe any similar obliterations on any of the documents which she produced for you?      A. Yes, I did.

Q. What was the nature of those documents?

A. They were the check stubs of the taxpayer, Mrs. O'Connor.

Q. Are those check stubs in your possession or to your knowledge in the possession of the Bureau of Internal Revenue at this time?

A. No, they are not in my possession and to my knowledge they are not in the possession of the Bureau of Internal Revenue.

Q. I show you a document dated July 8, 1946 and bearing the signature Catherine O'Connor, and ask you if that was originally produced here from the official files and records of the Intelligence Unit of the Bureau of Internal Revenue.

A. Yes, it was.

Q. Will you state the nature of that document without stating its contents? What type of document is it?      A. It is a signed receipt.

Q. That is enough. Thank you.

I am going to offer this in evidence as Government's next in order.

The Court: It may be admitted and marked.

(The receipt referred to was thereupon received in evidence and marked U. S. Exhibit No. 16.)

\* \* \* \* (Tr. page 85)

Mr. Campbell: If the Court please, pursuant to the Court's instructions, I have produced here the original of the anonymous letter referred to in the testimony yesterday, which I desire to submit to

the Court. I object, however, to the introduction of the original letter in evidence in that it bears certain handwriting which is possible of identification.

The Court: Pass it up.

(The document referred to was handed to the Court.)

Mr. Campbell: It is the third document of the group, your Honor. There is attached to it certain Bureau memoranda.

The Court: What is before the Court now?

Mr. Campbell: The defendant has asked for the right of inspection of the original document, to which I objected on several grounds: first, that it is a confidential communication, the author of which should be protected, there being certain handwriting on the original document; second, that it is immaterial to the issues here. As to the contents of that document, it is purely hearsay, and while it would be advantageous to the Government to have it in evidence, I am sure it is not the purpose of the defendant to seek inspection of the original document for the purpose of offering it in evidence.

Mr. Crittenden: I will offer it in evidence.

Mr. Campbell: Then the compared copy, the copy which has been prepared from it, is as good as the original, which might disclose the author of it and subject him to possible retaliation. It has long been the policy of the Government and their law enforcement agencies to protect the identity of informers. It is a privileged document.



Mr. Crittenden: Your Honor, the position of the Government and their witness is that that is anonymous and the signature on there is not the proper signature nor the address of the party who wrote it. They have made that investigation. So any objection stating the fact that it would disclose the party from the signature I think is wholly fictitious. Secondly, I think that the evidence is going to show that one of the Government witnesses was the party who actually wrote that, and I will tell your Honor very frankly there were three parties at the time that letter was written who knew that apartment house sold for \$17,000: Mrs. O'Connor, Mr. Hyman, her lawyer, who sold it to her, and her accountant. As far as our going into the question of the writing and who wrote or signed it, I am not even going to go into that question, but I think we are entitled to have that writing. It is very material to the defense of this case, and so far as counsel's statement is concerned, we do not intend to put it in evidence, I have the best intention of putting it in evidence and interrogating a number of witnesses about it. I think on the anniversary of Judas's betrayal it is probably fitting that is a very material point, and we are going to have that as one of our issues and one of our defenses in this case.

The Court: What purpose would it serve in this case?

Mr. Crittenden: It is going to show very definitely that this witness for the Government has a motive, which will be shown from its contents—

not the signature, but the contents of the instrument.

The Court: What relation has that to the guilt or innocence of this defendant?

Mr. Crittenden: It is a very material point. The one who told the Internal Revenue Bureau of the bearelaw was the one who wrote this, the one who turned her in, and the accountant the defendant relied on in this matter. It goes to the question of wilfulness. You will remember the great stress the Government placed on this matter, and this is certainly of the most material nature in view of the fact that we are going to show there were only three parties at the time that letter was written who actually knew the sale price of that property was \$17,000. There is one (indicating defendant), there is another (indicating Mr. Hyman), and there is the accountant who made up these reports with which she stands charged. Those are Government Exhibits 1, 2, 3 and 4 which she is charged with having filed. It is certainly material from our viewpoint.

Mr. Campbell: I am going to renew my objection and point out the privilege of such documents and suggest to the Court that the Court can seal the document in the event the Court has in mind or does sustain my objection, so if there is any question raised, it can be subsequently passed upon, that is, if the Court is in accord with my objection.

The Court: Is the matter submitted?

Mr. Campbell: Submitted.

Mr. Crittenden: Submitted.

The Court: The objection is sustained, and I will have this document sealed and turn it over to the Clerk so that both sides may urge their point hereafter to this. Proceed.

Mr. Campbell: At this time, your Honor, I wish to offer in evidence Government's Exhibit 14 for identification, it being the gray D.E. ledger.

Mr. Crittenden: That is only for identification?

Mr. Campbell: It is offered in evidence. It has previously been identified.

Mr. Crittenden: Your Honor, we will renew our objection and again state the grounds: It has not been proved since the 16th day of July 1942. We have no objection to the portions prior to that being admitted, but that part subsequent to the 16th day of July 1942 we object to as not being the record of the defendant. It was not shown nor is there any evidence showing it was kept by her in the regular course of business, that the business was of such a character that it is proper or customary to keep such a book, that the entries in the book are either original entries of the transaction or that the person making such entries, if they were made by the defendant, were made at her instance or request, or that the person who made it had personal knowledge of the transaction or obtained such knowledge from a report regularly made to him by some person employed in the business whose duty it was to make the report in the regular course of business. Having failed in that proof, we are putting in the objection on that ground, your Honor, and your Honor knows the

materiality from the prior trial of this case. We consider it an extremely important thing that that be proved if it is hers, and I thought it was proved the last time in the case it was not her writing, but Mr. Campbell is contending it was made by somebody for her in the ordinary course of business.

Mr. Campbell: I might state a full foundation has been laid for the book at this time. The evidence shows that this particular book, through the evidence of Mr. Divers, was kept by the defendant and himself in the regular course of business. The entries after July 16 to the 23rd of August are similar entries to those appearing prior to that date. Furthermore, there is the admission of the defendant, both orally and the evidence of Mr. Krause and in her affidavit that the entries with regard to the disbursements made in the business after the 16th of July are her entries or those of her husband. Some were hers and some were her husband's. I submit that that is sufficient foundation for the introduction of the document in evidence.

Mr. Crittenden: I think counsel has misstated the evidence.

The Court: The Court is aware of what the evidence is. The Court is prepared to rule. The objection is overruled. It is a proper matter to go to the jury.

(The book referred to was thereupon received in evidence and marked U. S. Exhibit No. 14.)

\* \* \* \*—Jost—(Tr. page 174)

Q. Now, after the default divorce, did you con-



sult a lawyer about the rights you had to that tavern?  
A. Yes, sir.

Q. It was a Mr. Edmond J. Hall, wasn't it?

A. That is right.

Q. Did he ask you to sign a pleading and to swear to it before a notary public?

Mr. Campbell: Objected to as immaterial, the legal rights of the parties having been established and determined by a court of competent jurisdiction in this state.

Mr. Crittenden: I think we can show that this man claimed, this lawyer advised him, that he had a right, and I will read it into the record, the verification.

Mr. Campbell: If the Court please, it is not what this man may have thought or believed. It is what the court has determined their rights were as of the time.

Mr. Crittenden: Well, Brown against Brown determined it, and you tried the last case on the basis of that suit, that he didn't have any interest.

The Court: What is this?

Mr. Crittenden: He signed a verified pleading drawn by Mr. Hall entitled "Answer to Complaint." in Jost against Jost:

"Answering the allegations of paragraph 5 of said complaint, defendant denies that there is no community property as a result of said marriage and in this behalf alleges there is community property consisting of certain stocks of liquor in the tavern business known as Kay's situated at 581 Valencia Street in

San Francisco, State of California, of the approximate value of \$9,000. The defendant further alleges—" that is the material portion.

Mr. Campbell: I call the Court's attention to the file which has been produced here, which shows the document was never filed. The default was entered, his motion to set aside was denied by the court, and the final decree was subsequently entered, which fully determined the property rights of the parties under the very case which counsel now cites and which he previously cited.

The Court: The objection is sustained.

Mr. Crittenden: Let the record show I want to make an offer of proof as to these matters.

The Court: You made your offer of proof. The record discloses it.

\* \* \* \*—Shannon—(Tr. page 197)

Mr. Crittenden: Q. Do they have wakes during the daytime at Dugan's?

The Court: We are not concerned with whether they have wakes or not. This is not the issue in this case. Confine yourself to the charge here.

Mr. Crittenden: I am showing the probability of his testimony.

Q. Do you have wakes in the day or in the night time?

The Court: The Court has ruled. Let it go out and let the jury disregard it.

\* \* \* \*—Shannon—(Tr. page 203)

Q. Your testimony as to how much there would be, for instance, over \$100, that is total cash that was in the drawer, wasn't it?

Mr. Campbell: Just a minute. Let me have that question read.

(Question read.)

Mr. Campbell: I object to that as assuming a fact not in evidence. He has not so testified, if your Honor please.

The Court: The objection is sustained.

\* \* \* \*—Shannon—(Tr. page 204)

Q. At that time you drank drinks during the day? A. Yes, sir.

Q. Approximately 20 drinks a day?

Mr. Campbell: Objected to as incompetent, irrelevant and immaterial.

The Court: What is the purpose of the testimony?

Mr. Crittenden: It goes to show the man's condition at the end of his shift as to his memory as to how much money was taken in or how much money there was in the drawer. He has testified to the amount of business there and I want to go to the weight and character of the amount.

Mr. Campbell: You have to know his capacity as well.

Mr. Crittenden: I think the jury would have to determine that.

The Court: Read the question.

(Question read.)

Mr. Campbell: Objected to as immaterial and incompetent.

The Court: Sustained.

Mr. Crittenden: Q. At the time you were working on these shifts to which you have testified you had had by the end of the day 20 drinks?

Mr. Campbell: Same objection. It is immaterial and incompetent.

The Court: Same ruling. The objection is sustained. If he was intoxicated or under the influence of liquor at any time and you are prepared to show it, the Court will allow it.

Q. And by the time you had been on the shift eight hours about how many drinks had you had?

A. Oh, around 20.

Mr. Crittenden: Q. And that was the regular size shots that was poured at the bar?

A. Yes.

Q. And you stuck to bourbon in drinking?

A. Yes, bourbon.

\* \* \* \*—(Tr. page 206)

Q. It was under the effect of those 20 drinks you say you could remember the volume of business?

Mr. McMillan: That is a loaded question.

Mr. Campbell: That is objected to as an incompetent question. It is compound and assumes a fact not in evidence.

The Court: Coupled with that, it is clearly argumentative. Let us have the reporter read it.

(Question read.)

The Court: The objection is sustained. Let it go out and let the jury disregard it for any purpose in this case.

\* \* \* \*—Bosserman—(Tr. page 222)

Mr. Crittenden: Q. Now, Mr. Bosserman, I ask you if you remember testifying upon the hearing on direct examination, page 85, starting at line 2:



“Q. Did you accept the figures in that regard as being accurate and correct?

“A. Well, no, I did not. Inasmuch as I had not audited Mrs. Jost’s books, I did not accept them as being correct. If I would come to something that did not look reasonable, I believe I eliminated it. For instance, there would be parties and so forth, and the thought in my mind was that maybe she could substantiate those by some documentary evidence. If I did not think she could, I just didn’t think it reasonable, and probably threw it out, and I may have done her an injustice.”

That runs from line 2 to line 11.

A. I made that statement.

Q. Will you examine that?

Mr. Campbell: Well, he stated he made that statement.

The Witness: Yes, I heard you reading that and I made that statement.

Mr. Crittenden: All right.

Q. You threw out a number of deductions she possibly could have taken, didn’t you?

A. Yes, where I felt there was no documentary evidence to support it.

Q. You gave the Government the breaks in making out the return, in other words?

Mr. Campbell: Just a minute. I object to the question in that form. That is putting words in the witness’s mouth and twisting his previous answer.

The Court: The objection will be sustained.

\* \* \* \*—(Tr. page 241)

Q. For which year are you referring, 1943 or 1944?

A. For 1943 and 1944—that last statement, yes, sir.

Q. At none of those times was there anything to put you on notice that these were not true and correct accounts you were working from and you were making a true and correct return from those?

A. You are asking for it. It did not look good.

Q. Did you tell her that? A. No.

\* \* \* \*—(Tr. page 266)

Q. I show you page 99, line 19 to line 23.

A. I guess that is correct.

Q. “Mr. Crittenden: Q. At the time you drew up these returns of 1942, 1943, and 1944 was there anything in the returns or the books that you were working from that would tend to lead you to believe that they were not correct?

A. No, there was not.”

Did you so testify?

A. If it is there, I did, yes.

Q. Do you want to reconcile that with the testimony that you gave before the noon hour?

A. I don't care to review my own testimony, no.

Mr. Campbell: To what testimony is counsel referring, if the Court please?

The Court: Read the last several questions and answers.

(Record read.)

Mr. Campbell: If the Court please, I distinctly remember the testimony. It was whether or not

he had a conversation after he was hired to keep books of account for her. He said, "Yes, I did. You asked for it. I told her she had accumulated too much wealth for the income tax returns that she had filed." That was at a period sometime after the filing of these returns. I recall that testimony very distinctly.

Mr. Crittenden: The testimony is—

The Court: The jury heard the testimony. Let them determine it. Let us proceed.

Mr. Crittenden: Q. Do you wish to reconcile the two?

Mr. Campbell: I object to that.

The Court: What is the question?

Mr. Crittenden: I will withdraw the question.

Q. Do you wish to explain—

The Court: Explain what?

Mr. Crittenden: The difference between this testimony read and what he gave before.

The Court: That is clearly argumentative. The objection will be sustained to the question.

Mr. Crittenden: May it appear in the record that I am impeaching the party—

The Court: The court has ruled. You proceed with this case.

\* \* \* \* —(Tr. page 249)

Q. You said you did not know which book you had gotten, or how you have gotten the figures together on the partnership return, but you must have had some book?

A. That is absolutely right. I don't remember the partnership return. I only remember very, very faintly making it up.

Q. You did not state you had not seen this grey book?

Mr. Campbell: Just a minute. Counsel is putting words in the mouth of the witness.

The Court: Read the question back.

(Question read.)

The Court: The objection will be sustained.

\* \* \* \* —(Tr. page 252)

Mr. Campbell: He has read it. I suggest the impeaching question be asked.

Mr. Crittenden: All right.

Q. Did you so testify as follows—

The Court: Q. Just a moment. Did you read that testimony? A. I read it, yes.

Q. Did you give that testimony as recorded there in the transcript?

A. I believe I did, all of that.

Mr. Crittenden: Q. You did give that testimony? A. I believe I did.

Q. You did state that she did state to you then she was surprised to find that it was taxable?

Mr. Campbell: Just a minute. I object to that. That is after her returns were in and it is not impeaching.

Mr. Crittenden: I asked, if your Honor remembers, as to the testimony that took place as to gambling and which he said was after the 1944 return. He stated all he did was to make the remark that gambling was taxable and she made no reply at all.

The Court: Q. At any event, the return was in at that time?



Mr. Crittenden: Yes.

The Court: What is the purpose of this testimony?

Mr. Crittenden: I am showing his testimony on cross examination was not complete and was not true when he said she made no reply.

Mr. Campbell: There is no showing it was the same conversation. That is counsel's conclusion.

Mr. Crittenden: I will read the entire testimony.

Mr. Campbell: I object to counsel reading.

The Court: I will sustain the objection. Reframe your question and develop any fact you wish in this case.

Mr. Crittenden: Q. Do you wish to explain the difference between the testimony you give now and what you stated before?

Mr. Campbell: Just a minute. That's objected to on the ground there has been no indication that there is any difference in his testimony on this occasion or any previous occasion.

Mr. Crittenden: Do you want me to have the reporter read back?

Mr. Campbell: No, that makes no difference.

The Court: The objection will be sustained.

Mr. Crittenden: Q. I will ask you if the next two questions—I will withdraw that question.

Do you remember at the time you testified at the last hearing, starting at page 96, line 6—

Mr. Campbell: Just a minute, please.

The Court: You will have to lay the foundation.

Mr. Campbell: I am going to object. The im-

peaching question must be asked first. I object to it in that form.

The Court: The objection will have to be sustained. Follow the rule.

Mr. Crittenden: Q. Did you make a statement in your testimony at the last hearing as follows:

Mr. Campbell: I interpose my objection, if the Court please.

The Court: Your objection will be sustained.

Mr. Crittenden: If your Honor please, I want to show a prior inconsistent statement and if you want me to show the statement I can do that.

The Court: You will have to lay the foundation to the introduction of that testimony.

Mr. Crittenden: You mean ask him what he has testified to?

The Court: What are you addressing those questions to, and for what purpose?

Mr. Crittenden: To impeach him by prior inconsistent statements.

The Court: Where is the impeachment?

Mr. Crittenden: Q. Mr. Bosserman, is your testimony that nothing was said at any time when you were preparing any of these returns or prior to the time you filed any of these returns as to the income from any of the various machines?

A. No, there was nothing said that I know of.

Q. That is your testimony on the prior part of this examination?

A. I don't remember what I testified to on the prior part of this examination, but it is my testimony now.

Q. I will ask you if you did not testify at the prior hearing—

Mr. Campbell: Will you refer to the page?

Mr. Crittenden: Page 96, line 6.

Mr. Campbell: Just a minute, before you read the question.

The Court: Is this the conversation had in 1945?

Mr. Crittenden: No, this is the testimony he gave at the prior trial.

The Court: I understand that.

Mr. Crittenden: (Reading “When you started to keep her books—”

Mr. Campbell: Just a minute, his impeaching question was laid prior to the filing of this 1944 return, and I submit, again beginning at line 22, page 94, it is shown that the conversation took place the latter part of 1945. There is no impeachment in the question counsel is asking. Counsel is attempting to draw attention to this by reading only a small portion of the question.

The Court: The Court is now prepared to rule. The objection will be sustained.

Mr. Crittenden: May I state the question before the objection is sustained?

The Court: What question?

Mr. Crittenden: I did not state any question yet.

The Court: If it be the fact it was in 1945, it was after these returns were in and filed.

Mr. Crittenden: The question does not refer to 1945.

The Court: I am only accepting counsel's statement for it.

Mr. Crittenden: Maybe I can frame a question and maybe it won't be for 1945.

The Court: Frame your question in any way you wish.

Mr. Crittenden: Q. Did you state at the former trial:

"Q. When you started to keep her books, do you remember talking about the income from the various machines with her?"

Mr. Campbell: I will stipulate he so testified, but such conversation took place in 1945 after he became her accountant. I submit the transcript in the former trial at line 22, page 94, should be read.

The Court: Read the last question.

(Question read.)

The Witness: I started keeping her books at the end of 1945, period. That is ended.

Mr. Crittenden: Q. Did you do any accounting work prior to 1945?

A. That is a matter of record—no.

Q. Not as a matter of record, as a matter of fact?

A. As a matter of fact, period.

Mr. Crittenden: May I have him answer the question that I propounded as to page 96, line 6 to line 8?

The Court: There is nothing before the Court, counsel. Proceed.

Mr. Crittenden: May I have a ruling?

The Court: There is nothing before the Court to rule on.



Mr. Crittenden: Do I understand that I have an adverse ruling on the question?

The Court: There is nothing before the Court, counsel. Proceed.

Mr. Crittenden: Will you read the question I asked the witness, and the answer?

(Record read as follows:)

“Q. Did you state at the former trial—

“Q. When you started to keep her books, do you remember talking about the income from the various machines with her?

“A. I started keeping her books at the end of 1945, period. That is ended.”

Mr. Campbell: I have already stipulated he so testified.

The Court: In any event, the record may stand as it is. Proceed.

Mr. Crittenden: I am in a peculiar position unless I have a ruling on this question.

The Court: Proceed. There is nothing before the Court to rule on. Proceed to the next question.

Mr. Crittenden: All right.

Q. Was anything said in any of your conversations with the defendant showing her belief that income from the music and other machines were already taxed by the Federal Government?

Mr. Campbell: Just a minute, I am going to object unless those conversations be confined to the period before or at the time the last return here in issue was filed.

The Court: The objection will be sustained.

\* \* \* \* —Bosserman—(Tr. page 261)

Q. This is your letter, your signature, is it?

A. That is right.

Mr. Crittenden: I am going to offer this in evidence.

Mr. Campbell: I object to it on the ground that no foundation has been laid. On the face of the documents they are remote, the documents having been written in 1947, relating to self-serving declarations made by the defendant in 1945, and the receipts referred to all being in 1947. I object to it as remote and no foundation laid, and also attempt to introduce self-serving declarations of the defendant made at a time after the completion of the crime, if any, in this case.

Mr. Crittenden: Your Honor, this letter—

Mr. Campbell: I think the letter should be submitted to the court rather than read in the presence of the jury.

Mr. Crittenden: It is to show in the record what it is.

The Court: Just a moment. Read the question.

Mr. Crittenden: I was just offering this in evidence, your Honor.

The Court: What is it?

Mr. Crittenden: It is a letter by Mr. Bosserman to Mr. Hyman dated July 25, 1947, with a statement on it that he had written it sometime ago and forgot to mail it. "I do not know whether it is any good, or not. Cy Bosserman." It is enclosed in an envelope with a postmark of November 17, 1947, and in it he states, "From my observation—"

Mr. Campbell: Pardon me, Mr. Crittenden. I

am going to object to the reading of this letter. The letter purports to have been written on July 28, 1947. It contains certain conclusions and opinions and refers to self-serving declarations made by the defendant in 1945 and in 1947.

The Court: Pass it up.

(The document referred to was thereupon handed to the court.)

Mr. Campbell: I make the further objection that it would be an attempt to invade the province of the jury.

Mr. Crittenden: It is used solely for impeaching this witness. It will go to the weight and veracity that the jury would attach to his testimony.

The Court: What is the purpose of this offer? To prove what?

Mr. Crittenden: I had asked this witness if his client had not disclosed to him that she had not the slightest idea of income tax or what was taxable and what was not, and he said she had made no such disclosure to him. Consequently, I am trying to show there that this man did know that she did not have the slightest idea—and it is another point that is extremely material in our case—that this client of his relied upon his professional services and acted in reliance upon them.

The Court: Do you wish to introduce this letter of July 28, 1947?

Mr. Crittenden: Yes.

The Court: Let the record so show. The court sustains the objection.

Mr. Crittenden: May that be marked for identification?

The Court: Let it be admitted and marked for purposes of identification.

(The document referred to was thereupon marked Defendant's Exhibit C for identification.)

Mr. Crittenden: Q. Did I understand it was your testimony before the noon recess was taken that you were not in the tavern the first time that you called and talked to the defendant and Mrs. O'Connor?

A. I believe I stepped in the door and asked where I could find Mrs. Jost, and they said. "Upstairs." I turned around and immediately went up.

Q. I will ask you to read your testimony on page 90, lines 8 and 9.

A. Line 8?

Q. Line 8 and line 9.

A. "Q. You went into the tavern?"

"A. That is right."

Q. You went into the tavern, is that your testimony? A. To find out where she was, yes.

Mr. Campbell: I am going to object to this method. Lines 6 and 7, which are immediately before that, read as follows:

"Q. Do you remember where it was?"

"A. Yes, I do now. It was in her apartment on Valencia.

"Q. You went into the tavern?"

"A. That is right."

The implication that counsel would leave here is that the witness is giving testimony that is contradictory.



Mr. Crittenden: That is up to the jury to determine whether it is different testimony. I think it is. I further would like to observe and have the record show that I assign as misconduct the attempt of counsel to argue before the time assigned for argument the questions of materiality of evidence and its weight, and the amount of weight that the jury should attach to it.

The Court: Let the statements of both counsel go out, and let the jury disregard it for any purpose in this case.

\* \* \* \* —Bosserman—(Tr. page 232)

Q. And when you went to her place of business you walked to the place of business, didn't you?

A. No, I went upstairs. She was upstairs.

Q. Didn't you talk to her downstairs at any time?

A. At any time—? Yes.

Q. When were you first employed?

A. Subsequently I did, yes.

Q. When was that?

A. I think two or three times in a period of two or three years.

Q. At the time you went in did you see the music machine in there?

A. I didn't notice them.

Q. Did you see the pinball machine or claw machine?

A. I didn't notice them.

\* \* \* \* —(Tr. page 350)

Mr. Campbell: You may cross-examine.

Mr. Crittenden: If your Honor please, this has caught me by complete surprise. There are a num-

ber of things he has covered on his direct examination in connection with his computations that are much out of line with the former computations and testimony we had. Your Honor will remember—

Mr. Campbell: If your Honor please, I object to this. I think this is highly improper.

Mr. Crittenden: I have to go into those questions.

The Court: You may bring those matters up in the absence of the jury. You may proceed with the cross-examination.

\* \* \* \*—Krause—(Tr. 322)

Q. Now, we will go into detail in each of the methods which you have used. With regard to the calendar year 1942, what was the amount your examination disclosed as having been the net taxable income of this defendant?

Mr. Crittenden: May I ask a voir dire question, if your Honor please, as to the man's qualifications on this?

The Court: Very well.

Mr. Crittenden: Q. I understood that Mr. Torrey made all the computations after your first. He made the second and third spread, isn't that correct?

Mr. Campbell: I object to that question. That is not a voir dire question. This man has shown his qualifications. I have no objection to any questions as to this man's qualifications as an accountant.

Mr. Crittenden: He has not made the computations.

Mr. Campbell: He stated he has.

The Court: You may take him over on cross-examination and ask him any questions that you wish.

Mr. Crittenden: Your Honor remembers the testimony at the former trial. Mr. Tormey is the one who made the computations.

The Court: You may develop that on cross-examination.

Mr. Campbell: Q. You made this audit, did you, Mr. Krause?

A. I personally made this examination to which I am testifying.

Q. When did you complete it, Mr. Krause?

A. The audit, here, oh, about a week or two ago.

\* \* \* \* —(Tr. page 447)

Mr. Crittenden: May I state to the Court, I asked Mr. Campbell and Mr. Tormey for an opportunity to examine the accounts, as your Honor suggested, during the noon hour, during the two hour recess. Neither of them gave me an opportunity to do it, and I wanted to show in the record that I have not had the opportunity to examine the work sheets and supporting documents for Exhibits 28, 29 and 30, which I intended to do during the noon hour.

The Court: My suggestion was to familiarize both sides with whatever data, whatever evidence was going to be introduced with the hope we wouldn't have to go over it in detail.

Mr. Crittenden: Yes.

The Court: Any statement or account that was not verified or what not; if you wanted to challenge it, that was my thought.

Mr. Crittenden: But I was denied the opportunity to do that, and I asked Mr. Campbell specifically at 12:00 o'clock to do that, and I asked Mr. Tormey and he said, "I can't do it, I will see Mr. Campbell," and he walked out the door and that is the last I saw of it, the last I spoke to them, before the case reconvened.

Mr. Campbell: Well, if the Court please, my understanding was that if counsel complained of any points of difference those things could be gone into. I have had none indicated. I have seen none. On prior occasions we have attempted, as counsel knows, to get together on those things—with absolutely negative results.

Mr. Crittenden: I think we got very positive results, and I wanted an opportunity to examine it, and I was denied that opportunity.

The Court: Well, in any event, there is nothing before the Court and that matter is entirely out.

Mr. Crittenden: May I have an order permitting me to examine those work sheets from which he has testified?

The Court: I issued an order in relation to any matter or writing that was in dispute, that it be available to you. I take it that Mr. Campbell is prepared to do that?

Mr. Campbell: I am, your Honor.

The Court: That is sufficient. Proceed.

Mr. Crittenden: May I see it as soon as the evening recess comes at 4:30?



Mr. Campbell: Well, if counsel will indicate to me where there is any dispute, we will be glad to go into that item. But to go over a three year audit item by item is impossible in the time at our command.

Mr. Crittenden: Well, very definitely in the original dispute—

The Court: There is nothing before this Court at this time. Proceed with this witness.

Mr. Campbell: That is all, Mr. Krause.

Mr. Crittenden: Well, may I have an order that that be turned over into evidence?

The Court: You will have no order, I have gone as far as I could go to give you any permission you wanted from this record. Indicate what item it is that is available or that you want made available to you.

Mr. Crittenden: I would like to have the work sheets, which showed the miscellaneous, those which are deductible, and the items in 1942—

The Court: Where are they?

Mr. Campbell: Mr. Krause, how many items approximately are included in your audit, a rough estimate?

A. Well, that is a little difficult to say. I think there are 40 lines to a sheet and well, it must be thousands at least, your Honor.

Mr. Campbell: And how many columns to a sheet? A. 14 columns to a sheet.

Q. And you have used a 14 column spread?

A. That is correct.

Q. And you have there five bundles of those

sheets, is that correct?      A. Three here.

Q. And how long did it take you to go over those items to list them?

A. Over two months.

Q. Over two months' time you have taken at that?      A. That is correct.

Mr. Campbell: I think your Honor can see the impossibility of going over item by item.

The Court: I think it would be well to cool off and let some air in the courtroom. I will allow the jury to retire for a recess.

(The jury then retired.)

(The following occurred without the presence of the jury.)

The Court: Now, then, for the purpose of the record.

Mr. Crittenden: For the purpose of the record, I wanted—

The Court: What items do you want?

Mr. Crittenden: Specifically there are two items in here of vast importance to me.

The Court: Yes.

Mr. Crittenden: One is the item showing detail in schedule on each of Government's Exhibits 28, 29 and 30.

The Court: Are those available?

The Witness: Yes, those are item by item listing of those disbursements shown in Mrs. O'Connor's books that were paid by cash. We compared every item in the book with the checks that were issued and those items not covered by checks; therefore, those are cash items.

The Court: Yes.

The Witness: And I listed each particular item regardless of size, 15 cents, 30 cents; so I have all those listed, month by month and totaled up. The total is the figure to which Mr. Crittenden refers.

Mr. Campbell: Q. That refers to some \$30,000 or \$31,000 worth of items, is that correct?

The Witness: Yes.

Mr. Crittenden: More than that.

Mr. Campbell: That covers \$30,000 or \$31,000 worth of items. Many of them are of a few cents, some are of several hundreds of dollars.

Mr. Crittenden: Now, then, the fact is this, the Government audit as shown in the prior figures shows that she had \$3,000 or \$4,000 less for the years '43 and '44 income chargeable to her than these accounts, and I want to go through and find out where the difference is in these, and the second thing I want to do, which the witness has testified he has in there, are the items which he has allowed and disallowed as applying to the various periods.

The Court: Well, we are going to take a recess. You can take the witness down on that table and he will point out any item that you wish to have him point out, so that you will be familiar with it.

Mr. Crittenden: Yes. Now, I want the record to show as well that the matter I wish to go into on this, on cross examination, was—

The Court: There is nothing now before the Court.

Mr. Crittenden: I want the record to show what the nature of my examination was.

The Court: Just a minute. I am conducting this hearing. The jury is absent here. Anything that goes in this record must be in their presence. The purpose of this inquiry was to assist you on any item that you wanted information on.

Mr. Crittenden: That is right.

The Court: Now, any matter that you are going to take up will have to be taken up in the presence of the jury.

Mr. Crittenden: Now, I attempted to make an offer of proof and your Honor precluded me, and I want to draw your Honor's attention to the transcript on December 23, 1947, at page 655, to the end of cross examination—I mean, on direct examination by Mr. Campbell of Mr. Tormey, and Mr. Tormey's statements as to what he did in the course of his work and investigation. And in this, if it was connected with the investigation, which this man was responsible for, and in charge of, and which he directed. And I wanted to go into that, which specifically shows the man's calling with a blonde girl and attempting to rent an apartment. Secondly, the calling at the place of business and the question of whether Mr. Tormey stated to the defendant that she could go to Mexico but that they would bring her back. Further, that he stated to her on leaving that night, after having three drinks, that the defendant would thank him for the report he sent to Washington. Also, the incident when Mr. Tormey sat at the bar drinking



with Mr. O'Connor and then with Mrs. O'Connor, went up to the apartment of Mr. Tormey and visited and saw the pictures. I think it is supremely material, particularly in view of this man's testimony that he directed and controlled the investigation and the manner in which it was conducted. And I have been precluded from going into any asking or questioning on the line of the conduct of this examination by Mr. Tormey, which was done at the direction and control of this witness.

Mr. Campbell: Those matters, if the Court please, if true, which I sincerely doubt, have no bearing on the issues of this case; and if at all admissible, they would only be admissible for the purpose of impeachment of Mr. Tormey. Mr. Tormey has not as yet, at least, taken the stand in this case. If there was any bias or prejudice on his part, that would possibly be admissible in cross examination. But it certainly is not admissible under the present state of the record, as counsel knows.

The Court: We will take our recess now.

(Recess.)

(Jury reconvened.)

(Tr. page 455)

Mr. Crittenden: If your Honor please, I covered from January to May, 1943 very hastily. I found six items—

The Court: I am not concerned with what you found.

Mr. Crittenden: Very well. There are a number of things I want to prove—

The Court: Just a moment. There is nothing before this court.

Mr. Crittenden: I want to go into this more thoroughly later on.

The Court: You can do what you like later on. The jury is here. Let us proceed with this case.

\* \* \* \* —(Tr. page 478)

Wednesday, March 31, 1948,

10:00 O'clock a.m.

The Clerk: United States vs. O'Connor, on trial.

Mr. Campbell: Ready.

Mr. Crittenden: Ready.

The Court: Waive the roll call, stipulating all the jurors are seated in the box. You may proceed.

Mr. Crittenden: If your Honor please, yesterday I asked that the papers used by Mr. Krause, and from which he testified, be produced and put in evidence. I have only seen them yesterday afternoon during the recess. I have not had an opportunity to examine them since then, and I would like to use them in the balance of the case, and I am sure the jury would be interested in them in their deliberations.

The Court: You may proceed. When the matter is presented I will dispose of it.

Mr. Crittenden: I am attempting to present it at this time, a request for that, and I would also like to have an opportunity to examine it, because that is largely the Government's case, and it differs very widely from the former testimony and very widely from the indictment in this case.

Mr. Campbell: I ask that the last statement of counsel be stricken and the jury instructed to disregard it.

The Court: Let it go out and let the jury disregard it. What is before the Court now?

Mr. Crittenden: I am renewing my request that those papers from which Mr. Krause testified on the stand be introduced in evidence.

The Court: Isn't the data already in evidence?

Mr. Crittenden: No.

The Court: Is the data available here in court?

Mr. Campbell: Mr. Krause will be here shortly, your Honor. He is not here yet. I sent him after some additional papers. May I state, if the Court please, that Mr. Krause testified here as to his findings in the matter. Counsel was given every opportunity to cross-examine at length and did so. I see no useful purpose in this request.

The Court: What I had in mind is this: Is the testimony that went in and the data pertaining to it available to counsel?

Mr. Campbell: Yes, it will be available as soon as Mr. Krause is here.

Mr. Crittenden: I certainly want to examine it and I want to put it into evidence.

Mr. Campbell: Are you offering it as your exhibit?

Mr. Crittenden: No, as part of the Government's case on cross-examination.

Mr. Campbell: If counsel desires to offer it in evidence I will have no objection, whatsoever.

Mr. Crittenden: I will offer it under Rule 43 (b) then.

Mr. Campbell: What is that?

Mr. Crittenden: An adverse witness.

Mr. Campbell: That does not apply here in a criminal case.

Mr. Crittenden: Sure it does.

The Court: The data will be available.

\* \* \* \* —Krause—(Tr. page 527)

Q. I will show you Defendant's Exhibit F, which are exemplars of writing by Mr. Krause on cross examination. He testified he wrote those words, "Call Int. Rev. Claw Mach." and ask you to examine that.

A. I would like to have some more of Mr. Krause's writing.

Q. In other words, you want something that he had written?

A. When he didn't know it was going to be used in court or for any other reason, just writing.

Mr. Crittenden: Could we have some of his work sheets that he prepared?

Mr. Campbell: You have one right here in evidence. May I have that exemplar of Mrs. O'Connor's writing?

Mr. Crittenden: I said Mr. Krause. No, I would like his work sheet, if he did some accounting work on it. May I have an order that that be produced? It is here in court lying on the desk.

Mr. Campbell: I submit that this expert has in his hands a document which was written in the court room in the presence of the jury. I do not know what more dignified an exhibit he could have.

The Court: What is before the Court?



Mr. Crittenden: A request that the Court order counsel for the prosecution to deliver to this witness for examination purposes all work sheets which are lying on the table there that were prepared by Mr. Krause and testified to by Mr. Krause.

The Court: Let the record show that your request will be denied. Proceed.

\* \* \* \* —(Tr. page 531)

Afternoon Session, Wednesday

March 31, 1948, 2:00

The Court: You may proceed.

Mr. Crittenden: If your Honor please, I asked Mr. Campbell again at the end of the morning recess to see those work sheets or to put them in evidence, that is, the ones Mr. Krause testified from, and I still have not seen them. Now, your Honor has indicated that I am entitled to see them.

The Court: To see what?

Mr. Crittenden: Those work sheets Mr. Krause testified from, those papers of account.

Mr. Campbell: I indicated to Mr. Crittenden that if he had any specific figures he wanted to inquire about, we would answer.

Mr. Crittenden: I told you the ones which we wanted, the deductions and how he arrived at the income.

The Court: We will now proceed with this case, gentlemen.

\* \* \* \* —(Tr. page 558)

PAUL W. TORMEY,

called as a witness on behalf of defendant; sworn.

The Clerk: Q. Will you state your name?

A. Paul W. Tormey.

Q. T-o-r-m-e-y.

A. Yes.

Mr. Crittenden: I am calling this man—

The Court: Mr. Krause has come in. Do you wish him now?

Mr. Crittenden: I got the names twisted, I am sorry.

I am calling this witness as an adverse witness under Section 43(b) of the Federal Rules.

Mr. Campbell: Now, just a minute. I object to that.

The Court: There is no application. Where is the rule? Have you it available?

Mr. Campbell: Are you referring to the Civil Rules?

Mr. Crittenden: Federal Rules of Procedure.

Mr. Campbell: Yes, Civil Rules.

Mr. Crittenden: Yes, and they are applicable.

Mr. McMillan: You are referring to civil or equity rules?

Mr. Crittenden: Do you have the rules there?

The Clerk: The civil rules?

Mr. Campbell: Yes, that is civil rules that you were referring to, I take it.

(Book handed to Mr. Crittenden by Clerk.)

Mr. Crittenden: Yes, 43(b) (Reading):

“A party may interrogate any unwilling or hostile witness by leading questions. A party may call an adverse party or an officer, director, or managing agent of a public or private corporation, or of a partnership or association which is an adverse party, and interrogate him by leading questions and contradict and impeach him in all respects, as if he had been called by the adverse party, and the witness thus called may be contradicted and impeached by or on behalf of the adverse party, also, and may be cross-examined by the adverse party, also, and may be cross-examined by the adverse party only upon the subject-matter of his examination in chief.”

The Court: The jurors may retire to take a recess for a few moments.

(The jury then retired at 2:48 o'clock p.m.)

(The following occurred without the presence of the jury:)

The Court: Now, we may clear this situation up in the absence of the jury.

Mr. Crittenden: My position is this: Mr. Tormey testified in the first trial as the Government's principal witness. Your Honor heard him testify. There were a number of things I am going to have to bring out from him. I cannot if I call him vouch for his testimony; and consequently the Government has not called him, as I had expected them to, and therefore when I put him on, I have to

bring out these facts and present it properly, present him, and I imagine his testimony will be much the same as it was in the first hearing.

Mr. Campbell: Now, if the Court please, I do not admit, in the first place, that this civil rule has an application as such to a criminal proceeding. And in the first place, Mr. Tormey is not an adverse party. That is clear. This is a criminal case brought in the name of the United States of America and Mr. Tormey is not a party to the proceeding. So that that portion of this rule, if the rule is applicable, would not apply. There has been no showing here whatsoever that this man is a hostile witness. As a matter of fact, his demeanor on the stand in the last trial indicated an effort at fairness and candor on his part. Well, now, Mr. Crittenden! He demonstrated candor and fairness on his part, so far as the defendant in this case is concerned. If the type question which I anticipate, which counsel intends to ask here—I don't presume or, may I inquire of counsel if he intends to go into the accounting testimony or if he intends to go into certain extraneous matters to which previous effort has been directed?

Mr. Crittenden: Both, both.

Mr. Campbell: Certainly this man cannot be put on the stand simply for impeaching purposes. Particularly with acts, if they occurred, which occurred long after the crime in this case, if any was committed. Furthermore, I do concede that there are cases in the Federal courts that hold that the court may, in its discretion, permit a witness



to be called and cross-examined without the party calling him vouching for him in any way, in which case the witness called is a court's witness. However, that is very seldom invoked, and in very unusual circumstances. Here there has been no showing, as a matter of fact, as I pointed out, it has been shown during the trial of the previous case that there has not been demonstrated any hostility by this witness toward the defendant. Now, if such should occur during the course of the examination, counsel may make application at that time, but until that time this witness, if placed on the stand, is his witness, called by him as announced by him prior to the recess.

The Court: I will adopt that procedure, namely, if this record indicates that he is a hostile witness, then we will take the position of taking him on as the court will rule. That will give you full opportunity to examine this witness.

Mr. Crittenden: I will assume to prove, as I did last time, I will prove how hostile he will be.

The Court: I can't anticipate what he will do. That is as near an interpretation of the rules as I am able to determine at this time, and that will be the ruling of the court. We will take a recess now.

(Recess.)

\* \* \* \* —(Tr. page 580)

Q. Were you present at all conferences with the defendant from—I should say at all conferences held between her and the Intelligence Unit from

and after your employment in this Intelligence Unit, or were there conferences?

A. So far as I know, I was at all the formal statements after December of '45, yes, sir.

Q. And after December of 1945 you made all of the investigation that was made? A. No.

Q. Somebody else did?

A. Well, as I have explained, Mr. Krause was doing certain matters, the deputy collectors were doing certain matters.

Q. This is your first case that you have been employed in by yourself, isn't it?

A. That is correct.

Q. And how many times did you see the defendant from and after your undertaking this case?

Mr. Campbell: Objected to as immaterial, if the Court please. After all, this is the defendant's witness. That has no materiality.

Mr. Crittenden: I am going to show what he did in this investigation. That is what I am leading up to.

The Court: I will sustain the objection.

Mr. Crittenden: Q. Did you go out to the defendant's place of business at any time?

Mr. Campbell: Objected to as immaterial.

The Court: Objection will be sustained.

Mr. Crittenden: Q. In the course of the investigation, did you go to the defendant's—did you talk to the defendant?

Mr. Campbell: Objected to as immaterial.

The Court: I will allow the question.

Mr. Campbell: It is also incompetent.

The Court: Did he talk to her? I will allow the question.

A. Yes, Mr. Crittenden.

Mr. Crittenden: Q. Now, will you relate to me the first time that you talked to her in the course of an investigation?

Mr. Campbell: Objected to as incompetent, if the Court please.

The Court: Incompetent in what respect?

Mr. Campbell: Well, Mr. Tormey is appearing here as the defendant's witness. It is an attempt to put in some self-serving declarations of the defendant. They are not admissible in this matter and I object to the conversation.

The Court: On that ground I will sustain the objection.

Mr. Crittenden: Do I take it as your Honor's statement that any—

The Court: The Court has ruled and you have a record here. We will have to proceed.

Mr. Crittenden: All right.

Q. In the course of your employment and investigation, did you have occasion to go out to the defendant's place of business subsequent to July of '46?

Mr. Campbell: Objected to as—

Mr. Crittenden: It may have been the fall of '46 or early spring of '47, January or February, 1947.

Mr. Campbell: Objected to as incompetent and subsequent to any date of the crime alleged to have been committed here.

The Court: I will sustain the objection.

Mr. Crittenden: Your Honor, I want to show under Rule 43(c), I want to show what the man did, as shown in the transcript starting with page 655 in Volume 7 on December 3, 1947. Specifically, I will show you the testimony, asked by Mr. Campbell of this witness:

“Q. —”

Mr. Campbell: Well, now, just a minute. If this is for any purpose of impeachment, the counsel can not impeach his own witness. I further submit that the offer of proof and the reading of a record of a prior case, the transcript of a prior record, has no place in this proceeding.

Mr. Crittenden: I will show the Court Rule 43 (c).

The Court: Very well.

Mr. Crittenden: (Reading).

“In an action tried by a jury, if an objection to a question . . .”

The Court: Just a minute. The Court is now prepared to rule. You have a record. I will sustain the objection.

Mr. Crittenden: Under Rule 43(c), which I am going to read, “In an action tried by a jury, if an objection to a question propounded to a witness is sustained by the Court, the examining attorney may make a specific offer of what he expects to prove by the answer of the witness.”

Specifically, I want to show that he would testify as follows—

Mr. Campbell: Now I am going to object to



this, if the Court please. The Court has overruled an offer of proof.

The Court: I trust that you will try to comply with the ruling of the Court. I am usually able to get along pretty well under circumstances such as this without very much difficulty—under circumstances not only of this kind but all others. I allow the widest latitude in every case. You have a record in this case. If I am in error, you can take advantage of it.

Mr. Crittenden: Under Rule 43(c) I am required to do what I am here attempting to do. The language of it is very clear. I will show you two Supreme Court cases and one Circuit Court case in this Circuit.

The Court: You frame your questions and I will rule on them and that way you will have a record.

Mr. Crittenden: Q. Mr. Tormey do you remember being called to the stand by Mr. Campbell in the prior case on December 3, 1947?

A. I know that I was called to the stand. I can't recall the date at this time.

Q. Do you remember Mr. Campbell asking you some questions about going out to the defendant's place of business? A. Yes.

Q. Do you remember the instance to which they referred? A. No.

Q. Do you remember the incidents when you went out with a blonde girl to rent an apartment, in the testimony that you gave on direct examination asked by Mr. Campbell?

Mr. Campbell: I am going to object, if the Court please; first, this is an attempt to impeach his own witness. Further, I call the attention of the Court to the fact that counsel has persisted in this line of questioning despite the rulings of the Court.

The Court: The objection will be sustained.

Mr. Crittenden: Q. Do you recall testifying as to a time that you went out there to the defendant's place of business?

Mr. Campbell: Same objection, if the Court, please.

The Court: The objection will be sustained.

Mr. Crittenden: Q. Do you remember the testimony you gave relative to the time you brought a blonde girl up to the defendant's apartment?

Mr. Campbell: I am going to make the same objection, if the Court please.

The Court: The objection is sustained and at this time I admonish the jury that this blonde girl that reference is made to, they will disregard that. It may go out and the jury will disregard it for any purpose of this case. You may proceed.

Mr. Crittenden: Now, I understand from your Honor's statement in chambers after the last trial that I was to ask questions until it was thoroughly established that a valuable right has been denied me, and in that suggestion I am going to continue to ask these questions.

The Court: Now, you will desist with the order of the Court. That is clear to you, isn't it? You see, I am responsible for the conduct of the trial of

this case in this court. You have a record here to protect you in the event that you determine that I have denied you any of your legal rights.

Mr. Crittenden: Well, I have to show that under Rule 43(c), what I intend to prove.

The Court: The Court has ruled. You have a record.

Mr. Crittenden: May I have the record show that I stated that I intended to prove that in 1946—

The Court: I admonish you at various times that what you propose to prove we are not here concerned with. You attempt to prove it and I will rule.

Mr. Crittenden: May I have the rules of the Court, 43(c)?

The Court: Now, for the purpose of the evidence, it is not necessary to read the rule. You can indicate.

Mr. Crittenden: May I point out to your Honor what I am trying to do so that I can have this record to show that I am doing what this rule tells me to do?

The Court: The number of the rule is sufficient for the purpose of the record.

Mr. Crittenden: Well, then, under that rule, I am required to make my statement of what I intend to offer, an offer of what I expect to prove by the answers of the witness.

The Court: There is nothing before the Court. Frame your question and I will rule on it.

Mr. Crittenden: All right.

Q. Do you remember the time you discussed renting an apartment from the defendant?

Mr. Campbell: I object to that as immaterial and an attempt to impeach his own witness.

The Court: Objection sustained.

Mr. Crittenden: Under Rule 43(c) I wish to show that this witness went to the place of business, spoke first to the defendant's sister and later to the sister herself, and then discussing the renting of an apartment—

The Court: Now, you will desist from any further comment in relation to that matter. The Court sustained an objection to it.

Mr. Crittenden: Pardon me just a minute, your Honor.

The Court: It is now time for the jury to retire. You may be excused until tomorrow morning at 10:00 o'clock. The jurors may be excused.

(The jury retired at 3:59 p.m.)

(The following then occurred without the presence of the jury:)

Mr. Crittenden: I want to draw your Honor's attention to the decision in the case of Sacramento Suburban Fruit Lands Company v. Soderman in the Ninth Circuit, reported in 36 Fed. 2nd 934, in which the Court points out that if a witness is asked if he knew the value of Minnesota property and the Court erroneously sustained the objection—but the report does not indicate what was expected to be proven, and the answer might prove unfavorable to the appellant, and consequently the error is not presented on the record unless the lawyer presents and states under Rule 43(c) the particular substance of the testimony.



I want to point out further to your Honor the decision of *Herencia v. Guzman* in 219 U. S. 44, 31 Supreme Court 135, and 55 Law Edition 81; in which, being an action for negligence, the testimony of a witness, physician, was excluded. The Court held that it could not set aside a judgment, because of a ruling on the evidence, where it does not appear that the evidence, what evidence the physician expected to give.

And further on, the case of *Scotland County v. Hill*, 112 U. S. 183, 5 Supreme Court 93, 28 Lawyers Edition 692, which was a proceeding in equity by a taxpayer to test the validity of stock subscriptions to a railroad company and the power of the County Court to bind the County to pay the bonds. The Court held that error can be assigned in a Court on an exception to exclusion of evidence on oral offer to prove facts; although the record does not show the witness was actually called to the stand to give the evidence or anyone was present to be called for that purpose.

And I want to come within the direct rule of those cases in protecting my record here. I am required, as I understand, by the rules and the decisions of the courts to do that. In all due respect to your Honor, I must protect the rights of my client.

The Court: You have a record now.

Mr. Crittenden: I want to show that this witness, while in charge of the investigation, and which he testified in the former trial was in the course of an investigation, went with a blonde

girl to the apartment house of the defendant O'Connor, that he went upstairs with this girl and that she undertook to rent the apartment from the parties; that there was a disagreement and this man did not think the rent was proper; and furthermore, that he contends that the furniture was included in the rental; and that they went downstairs and left, he claiming that the husband of the girl waited outside in the automobile; that he was on his day off on that particular day and that he left them to take a taxi elsewhere. We can prove by testimony that there were other circumstances, including the statement at the time that the girl did not think the bedroom in the apartment was sufficiently private. I also wish to go into the time that this defendant was at the bar engaged in her business and Mr. Tormey came to the bar and asked to talk to her, had some drinks, and when he left, in the presence of her, in the presence of one of the witnesses which we called for last time, and her sister, made certain statements. One was the question which the witness will deny, that he told them that they could go to Mexico but if they did they would be brought back. Also at the time of leaving, in the presence of the defendant and her sister, stated that the defendant would thank the witness for the report he sent to Washington in the case he was investigating. And I will show further that this man came into the bar, had some free drinks, talked to the defendant's then husband, Mr. O'Connor; that they went to his apartment and visited and that some

drinks were had, although I understand it is this man's position that Mr. O'Connor did not have anything but Coca-Cola; that he showed pictures of his war experiences or where he had been during the war to the parties, invited them to return some time when his wife was there. Now, that is the nature of the testimony I want to go into in this case, your Honor.

The Court: And the purpose of that testimony is what? What is the purpose of it?

Mr. Crittenden: The purpose is to show the nature and the character of this investigation, how it started, how it was based, upon what motive, not only of this witness making his reports on which the prosecution was carried on and which was discussed at length by a witness of the Government as to how it was reviewed, but also—

The Court: The motive—what did you have in mind when you indicated “motive”? Motive for what?

Mr. Crittenden: Well, I should say that the least that would be said of the conduct of this witness was that it was reprehensible and vicious and it would certainly show the nature and the extent of the investigation and what was done and what was before the reviewing authorities of the Penal Division of the Treasury Office; and again when it was reviewed at the Justice Department, which was made quite an issue and gone into by Mr. Campbell on examination of his own witness. And I also think that it would show the weight and character that should be attached to Mr.

Krause's testimony, who was in charge of this investigation when these things were being done by a person under his direction and control, and for whom he was responsible and would undoubtedly influence the facts, in weighing his testimony.

The Court: I will hear from the Government, for the purpose of the record.

Mr. Campbell: If the Court please, in the first place, the civil rule to which counsel alluded, I understand is expressly precluded from application to criminal cases. However, even though it were applicable, it certainly has no provision here. The defendant has seen fit to call Mr. Tormey as her witness. Now, with this testimony to which he has referred and which, from counsel's statement, was made subsequent to any acts on the part of the defendant, they would only be admissible if they were for the purpose of showing bias and prejudice on the part of this witness, whom they have called—and therefore they would be impeaching him. The rule is too well known that one can not impeach their own witness unless they are taken by surprise by his testimony, in which case they can show prior contradictory statements. There has been no showing of prior contradictory statements, and if there were, they could not impeach his testimony by this type of showing. They would have to show prior contradictory statements as to the accounting evidence which he has given here. The testimony is clearly inadmissible. It has nothing whatever to do with the facts of the case, although counsel has seen fit throughout the trial to make



insinuations concerning it. Your Honor having ruled on the matter, and I hope that your Honor will again rule that the evidence is clearly inadmissible, I think counsel should be admonished from attempting time and again in the presence of the jury to interject such an issue here.

The Court: Well, I want him to have a whole record on that.

Mr. Campbell: I understand, your Honor.

The Court: So for the purpose of this hearing, the Court is now prepared to rule, and for the purpose of the record, so that you will have a record, I will sustain the objection.

Mr. Crittenden: I take it by your Honor's ruling, so that I may be bound thereby, that any further inquiry as to the manner or nature or character of conducting this investigation is not admissible and would not be proper for me to go into that on the examination?

Mr. Campbell: We don't ask for such a ruling.

The Court: No, I can't anticipate what you are thinking about or what you have in your mind. We will have to proceed orderly in accordance with the rules.

Mr. Crittenden: Well, the point is this: Your Honor has heard the testimony in the prior case where I put on both, with the three witnesses as to how this investigation was conducted, and the statements of the investigator in the Court as to his investigation. I have the best of intentions of putting on and giving the jury the facts of the case, which are material to show how this material was conducted.

The Court: Well, I suppose if there were any criticism at all, it should be directed at the Court. I allowed, as I try to allow in every case, wide latitude; and I am free to say that I went beyond any reasonable bounds when I permitted you to do that. There is nothing unusual about that, for I do it repeatedly. You will have a full opportunity to be heard when we are through with this record.

Mr. Crittenden: Yes, but if your Honor—

The Court: I shall bind you to nothing. We have to confine ourselves to the rules.

Mr. Crittenden: Well, if your Honor takes the position that these matters which I put on at length in the last trial are not admissible, I don't want to go into the questioning and presenting of the witnesses and interrogating them on the stand. And on the other hand,—

The Court: I don't think that any of these visits to the apartment with the hope of renting an apartment have any relation at all to the issues involved in this case.

Mr. Crittenden: Well, if your Honor's ruling on the question—

The Court: Is that sufficient record for you?

Mr. Crittenden: That is sufficient.

The Court: Very well.

Mr. Crittenden: Now, it is—

The Court: It is now time for adjournment.

Mr. Crittenden: May I have some kind of an order to be able to examine the records of Mr. Krause from which he testified?

The Court: My experience here has been, for

some period of time, that you would have no difficulty in getting any information you wish from the Government, for I have never knowingly known of any case where they didn't give any information within any reasonable bounds with relation to what they have. I trust that is true here. I have no reason to believe it is not true.

Mr. Crittenden: Your Honor, it is not true in this case.

The Court: Well, you will have to point out what you wish.

Mr. Crittenden: I wish to have the statement of the work sheets which show the disallowed items, those which were not given as a deduction to which Mr. Krause testified he had marked in his work sheets; and I also want to find out the papers and sheets on which he computed this far greater sum than Mr. Tormey.

The Court: We are concerned here with the ultimate fact, whatever it might be.

Mr. Crittenden: I want those—

The Court: If we went into every work sheet making up these various accounts, why, I am afraid this jury would be quite uneasy about it. It would take weeks. I don't see how it could be done.

Mr. Crittenden: It is obvious that this man's testimony, Mr. Krause's testimony, is wrong. It is wrong even by his own assistant's account as to the gross receipts. And the method of accounting that was used was pointed out by this accountant to be probably subject to overstatement.

The Court: Well, I can't stop you from think-

ing. You can think as you please, and I am not going to interfere with you. But I will give you a record on anything you want here and there is now nothing before this Court. So we will now conclude for the day.

(Thereupon an adjournment was taken until tomorrow, Thursday, April 1, 1948, at 10:00 o'clock a.m.)

\* \* \* \* —Tormey—(Tr. page 598)

Mr. Crittenden: Q. I will have to take it in this way. I will have to take each of these items and have you show me where you entered them in the book. For instance, that music, 15 cents, under the February miscellaneous column, will you show me where that is.

A. I can do it. It might take me some time to find it.

Mr. Crittenden: I will state to the Court, to save time on this, that we have gone over these things and he did carry them by month.

Mr. Campbell: I suggest counsel ask the direct question, if the Court please. This man here is his witness and not subject to cross examination by counsel.

Mr. Crittenden: He is slightly hostile when he answers differently than he did before.

Mr. Campbell: I object to that and ask the Court to instruct the jury to disregard it.

The Court: It may go out and the jury is instructed to disregard it.

What 15 cent item do you have in mind? What is the importance of it?



Mr. Crittenden: I want to show, your Honor, in these columns as he took them off he took them off as totals, and we can't reconcile them as to the figures at all.

Mr. Campbell: Objected to as an attempt to impeach his own witness.

Mr. Crittenden: I want to show the type of computation that the Government has made.

Mr. Campbell: These are computations, if the Court please, that are now being advanced by the defendant as being the correct computations.

Mr. Crittenden: I am not advancing them as the correct computations. I am trying to show just what the Government acted on, the basis of their report.

Mr. Campbell: Counsel has seen fit to make this man his own witness and I submit he is bound by his testimony.

Mr. Crittenden: I had to because you failed to call him. You had him on the stand at the last trial.

The Court: We will get through with this 15 cent item and then the Court will be prepared to rule.

Mr. Crittenden: Very well.

The Witness: The item of 15 cents to which Mr. Crittenden has directed my attention appears in the defendant's book in column 10 labeled "Miscellaneous," bearing a total of \$13.95 for the entire column. The addition of this column was corrected to a total of \$13.98 and allowed in my audit as general expense.

Q. Will you show me where that item of 15 cents is entered in your book?

A. Yes, I just testified it was allowed as general expense, the total amount of \$13.98.

Mr. Crittenden: The witness is pointing to a line of a total of \$13.98 on his work sheet.

Q. There is no breakdown, then, on these various items, is there?

A. Yes, it is identified on my work sheets as appearing in Taxpayer's miscellaneous column 10 of the photostat.

Q. Let us take the month of March. We will take the first item up here, Bosserman filing income papers, \$45. Will you find that for me?

Mr. Campbell: Objected to, if the Court please, as immaterial, incompetent, and an attempt to impeach his own witness.

The Court: The objection is sustained.

Mr. Crittenden: May I have him show me where the item of paper for door, \$1.36 is?

Mr. Campbell: Objected to as incompetent and an attempt to impeach his own witness.

The Court: Let him show it if there is any question about it at all.

Mr. Crittenden: Q. It says "paper for door, March 2, \$1.36."

A. The item labeled "paper for door" in the amount of \$1.36, appearing in column 10 of the taxpayer's record for the month of March 1943, appears in a column which I have correctly totaled to the sum of \$331.76 and is charged as personal drawings of the taxpayer, every item in that ac-

count, for the purpose of my audit having been considered a non-deductible expense.

Q. You retotaled these to \$331?

A. That is the figure which I entered in my work sheet.

\* \* \* \*—Tormey—(Tr. page 605)

Q. Supposing I add these together and see what they come out to.

Mr. Campbell: Objected to as an attempt to impeach his own witness and certainly developing no issue with respect to this case.

The Court: The objection is sustained.

Mr. Crittenden: Your Honor, the mathematics in this case will show that there has been terrible mistakes in mathematics, and the basis of the Government's case—

Q. The "paper for door, \$1.36" is included, according to your testimony, in the total of \$331.76?

Mr. Campbell: Objected to as an attempt to impeach his own witness.

The Court: The objection is sustained.

Mr. Crittenden: I want to show the type and nature of the Government's computations on which they have based their case. \$346.30 is the total of this column and I want to show the arithmetic is entirely wrong, that the man has taken totals and has not used them properly.

Mr. Campbell: I ask that that be stricken.

The Court: Let the remarks of counsel go out and let the jury disregard them for any purpose in this case. We will proceed with this case.

Mr. Crittenden: Q. May I have that arithmetic total? You are an accountant, aren't you?

A. I have so qualified.

Q. Will you give the arithmetic total of these figures in this column 10 of March 1943?

The Court: Have you got them?

A. No, I don't have them.

Mr. Campbell: Objected to.

The Court: In any event, he hasn't got them.

Mr. Crittenden: We can get them. It is a simple arithmetic problem.

The Court: Take that book down and proceed with this case. Now, I warn you, so you won't be taken by surprise. You obey the order of the Court.

Mr. Crittenden: I have always obeyed the order of the Court.

The Court: I will see to it that you do. I only say that kindly to you at this time. It has never at any time become necessary for this Court to punish anybody because they did not obey the Court. I have a duty here. There is a jury sitting in this box, and I want your client and everyone else who is charged with an offense coming into this court, to have a full opportunity to present their matters to the jury, but they must do it within the rules, and you are familiar with the rules.

Mr. Crittenden: Yes, your Honor.

The Court: Now, you proceed, and that will be sufficient for all purposes of this case. You now proceed legally.

Mr. Crittenden: Q. May I have the items of January 1943 that are shown in this column No. 10? Show me where they are entered in your work sheet.



Mr. Campbell: Objected to as immaterial.

The Court: The objection will be sustained.

Mr. Crittenden: Q. May I have the item of "Fix chair and globes, \$3.30," appearing on January 9, 1943.

Mr. Campbell: Objected to as incompetent.

The Court: The objection is sustained.

Mr. Crittenden: Will you show me where you have entered and how you have carried the item of \$15 under miscellaneous on the 15th day of January 1943 that is marked "Mops, brooms, paints, et cetera."

Mr. Campbell: Same objection; further, that is an attempt to impeach his own witness.

The Court: Same ruling. The objection will be sustained.

Mr. Crittenden: May I have the record show I am looking for a particular item appearing on the black book, the book of account.

\* \* \* \*—Tormey—(Tr. page 621)

Q. Now, if all the disbursements in the black book were added together, what more would you have to add to it to arrive at the sum of \$15,971.07?

A. Now, you are restricting your question to the black book, and my answer is, I don't know.

Q. Did you get any data for the year 1942 other—I am referring to July 16 until the end of the year. Did you get any data outside of that black book, as items paid by cash?

A. Yes.

Q. What were they?

A. Oh, items paid to Brady's Jewelry Company.

Q. In 1942 I am referring to.

A. Oh, no, I can't answer that question anyway, because I didn't make any effort to secure any outside payments other than the books, the checks and known records with her suppliers. We made contra audits, I mean audits of the contra accounts with all her liquor supplies and Lachman Bros. Furniture and everybody, we know she had done business with. And those, Mr. Hyman, those records were all that I made any endeavor to use. I realize she spends out large sums for her personal use and living expenses, but they did not enter into these calculations.

Q. I am trying to find out how I would arrive at this sum of total items if I used the evidence that is before this court in the black book, of the checks and the answer is I could not do it. Is that correct?

A. No, the answer is not that.

Mr. Campbell: Just a minute. I am going to object to that question because he limits it to certain exhibits, and then he says the evidence before this court. There is other evidence before this court which these men have testified to that they took into consideration. I suggest that the question is misleading for that reason.

The Court: The objection will be sustained.

\* \* \* \*—Tormey—(Tr. page 640)

Mr. Crittenden: I have a question or two. I want to state to the Court before I start in that I am greatly surprised in this: At the time we asked for a bill of particulars, particularly on September 2, 1947—

The Court: Just a moment. You proceed with this witness. I am not concerned with what you have in mind. This witness is on the stand. Examine this witness and proceed to do it now.

Redirect Examination

Mr. Crittenden: Q. Mr. Tormey, you say the ordinary audit requires external verification in addition to the books and records?

A. Wherever it is possible, yes.

Q. You go out and make an independent investigation?

A. It is left to the judgment of the investigating officers.

Q. You go out and make independent investigations?

A. Oh, yes, we check bank accounts, we check the accounts of vendors or wholesalers or department stores. That is customary procedure.

\* \* \* \*—Alberta Beall—(Tr. page 650)

Q. I point out Mr. Tormey sitting in the back section over there. Do you know him?

A. Yes, I have waited on him at one time.

Q. In 1946 can you give the date when you saw him, waited on him?

A. I can't give the date. I don't remember the date.

Q. The approximate time. Can you give me the month?

A. I don't know what month it was in. It was on Friday, Saturday or Sunday because those were the only three days I worked.

Q. Do you remember an evening when he came in the bar?

Mr. Campbell: Objected to as incompetent, irrelevant and immaterial and remote, and has nothing whatsoever to do with the issues of this case.

The Court: The objection is sustained.

Mr. Crittenden: Q. Referring to a time when he and the defendant met at the bar, do you remember an instance when that was?

Mr. Campbell: Just a minute. That is objected to as incompetent, irrelevant and immaterial.

The Court: The objection is sustained.

Mr. Crittenden: Your Honor, I am seeking to go into the line of questioning I went into in the former testimony of this witness in the former trial of the case. If your Honor wants to rule on that, that that is not competent—

The Court: The Court has already ruled. The record is here. Proceed with this witness.

Mr. Crittenden: Q. Did you hear anything that Mr. Tormey said to the defendant that night when he came in the bar?

Mr. Campbell: Objected to as immaterial, irrelevant and incompetent.

The Court: The objection is sustained.

Mr. Crittenden: Q. What was the first thing Mr. Tormey said that night?

Mr. Campbell: Same objection.

The Court: Same ruling.

Mr. Crittenden: Q. Where did he sit?

A. Second—

Mr. Campbell: Same objection.

The Court: What was that?

A. He sat in the second booth.



\* \* \* \*—(Tr. page 652)

Mr. Campbell: I had interposed an objection at that point. I ask that the answer be stricken.

The Court: The objection is sustained. Let the answer go out. It will be disregarded.

Mr. Campbell: And I object on the ground it is incompetent and irrelevant.

Mr. Crittenden: Q. What, if anything, did Mr. Tormey say to you at that time?

Mr. Campbell: Same objection.

The Court: The objection is sustained.

Mr. Crittenden: Q. Did the defendant, Mrs. O'Connor, buy or order any drinks at that time?

Mr. Campbell: Objected to as immaterial.

The Court: Objection sustained.

\* \* \* \*—(Tr. page 653)

Mr. Crittenden: Q. Which season? Was it spring, winter, summer or fall?

Mr. Campbell: I think that is immaterial. If the conversation took place in 1946, it is remote to any event that has been committed here.

The Court: I sustain the objection to this line of testimony.

Mr. Crittenden: If your Honor is ruling we can't go into that—

The Court: The Court has ruled. You have a record here sufficient for all purposes.

Mr. Crittenden: Q. Did Mr. Tormey make any statements at the time to which you are testifying?

Mr. Campbell: Objected to, if the Court please, and to further questions along this line, it having been demonstrated the conversation, if any, was in 1946.

The Court: The objection is sustained.

Mr. Crittenden: That is all.

\* \* \* \*—Tormey—(Tr. page 638)

Cross Examination

Mr. Campbell: Q. Mr. Tormey, on direct examination you stated that your audit was made in conformity with the general Bureau of Internal Revenue audit. What did you mean by that?

A. That is so far as possible we would substantiate all income and all expenses and allow such matters as are provided by law to be allowed.

\* \* \* \*—(Tr. page 646)

Mr. Crittenden: If your Honor please, I want it to appear that we made a motion for a bill of particulars and it has just come to my knowledge, despite the testimony of Mr. Siegel, Richard Siegel on September 2, 1947, on the motion for a bill of particulars, that the entire case was restricted to and was based upon the books of account of the defendant, the testimony now shows that not only was it not restricted to that but it is a general practice of the Intelligence Unit to go outside and make independent investigations, which if they believe is substantiated by proper evidence, they take and we do not and have not been able to determine or had before us for the preparation of this case any of this evidence which the Government has shown in their testimony, or at least the Government witness has shown in his testimony—we called him here—are matters not in the defendant's records or matters of independent investigation being used in the determination of these amounts. I will state

to your Honor it is a great surprise to me, and I have proceeded in this trial with the assumption that these computations were based solely upon the books of the defendant and the statements of the taxpayer and not upon additional investigations which we have no knowledge of, and I have asked to see these accounts of the Government, and I am sure if we go into that now, from the statement of this witness we would undoubtedly find where there is other or additional matter which is the result of this investigation to which has been testified.

Mr. Campbell: If the Court please, this is a rather late date for counsel to claim surprise after he has gone through the original case. As to his assertion, I was not present at the time he refers to when the request for a bill of particulars was made. However, this witness, for example, has testified his audit was based on these books and records and her statement of discrepancies, that he attempted to substantiate the matters made in her record and then submitted those things to her, where he thought there was a discrepancy between the books and records and she then signed the statement. We have been through all the evidence in this case. I have seen nothing which has taken counsel by surprise. He has indicated by his questions here that he is thoroughly familiar with the Government's case, and so I respectfully submit that the motion should be denied.

The Court: Denied.

\* \* \* \*—Mrs. O'Connor—(Tr. page 724)

Q. Now, did you have occasion to do any entertaining for various people or customers in the bar?

A. Yes, I always entertain. The only time I got a chance to entertain, because we were always working, was after we closed at night.

Mr. Campbell: If the Court please, I do not believe there is any issue as to entertainment. Mr. Krause stated that anything listed as entertainment in the book, he allowed in his schedule here.

Mr. Crittenden: I don't think that that is the fact, that they are all allowed. I think I have got to go in here and show the financial transaction. I have asked Mr. Campbell for the exact figures on these, which were allowed, and disallowed.

The Court: I have repeatedly instructed the jury to disregard any statements made by counsel on either side. It is not evidence and has no place in this case. Let us proceed with this case.

\* \* \* \*—Mrs. O'Connor—(Tr. page 755)

Q. When did you start paying her the \$30 a week?

A. I gave her \$30 a week when she was here. My sister helped me wonderfully in the club up there at 581.

Q. What did she do in the club? What were her duties?

A. She was all around. She spent 75 per cent of her time downstairs.

Q. What did she do downstairs?

A. She would make up things.

The Court: We are not concerned with what she did.



Mr. Crittenden: I want to show the services she performed.

The Court: If she performed services and got paid for them, we are concerned with what she was paid.

Mr. Crittenden: What did she do that she was paid this \$30 for?

A. She made up syrups, she cleaned the back bar, she would help me at night.

The Court: What relation has that, the nature of her work?

Mr. Crittenden: There are a lot of expenses like, for instance, the traveling expenses of the sister—

Mr. Campbell: There is no issue of that, if the Court please. We have allowed the traveling expenses. We have allowed the sister's salary. We are going into matters on which there is no dispute.

Mr. Crittenden: Your Honor, I have no way of knowing that. I have asked for an opportunity to see those papers and it has been denied me consistently. I have seen them for just one recess on, I think, one day.

The Court: You only have to see it once.

Mr. Crittenden: I haven't had much time over it.

Mr. Campbell: During the course of the other trial, we spent two days with counsel going over these matters. Counsel has had a full right of cross examination not only of Mr. Krause, who made those, but he put Mr. Tormey on the stand, and went into a number of these items and determined whether they were allowed or not.

The Court: The court has not concluded the calendar. There are other matters on the calendar. I will excuse the jury at this time for a recess.

\* \* \* \*—Mrs. O'Connor—(Tr. page 761)

Q. The time you separated from your husband in July of 1943.

A. I just had the car, and I had my business.

Q. And you had some money in the bank?

A. And some money, whatever was in there, yes, sir.

Q. Did you owe some current bills at the time?

A. I always owe bills.

Q. Approximately how much did you owe at the time, will you state that?

Mr. Campbell: Objected to as immaterial.

The Court: Objection will be sustained.

Mr. Crittenden: I want to show that the allegations of the community property are—

The Court: The objection is sustained. Now you may proceed.

Mr. Crittenden: Q. When you filed your action for divorce, who did you employ for your counsel?

A. Mr. Hyman.

Q. Did you discuss the allegations of community property with him at the time?

Mr. Campbell: Objected to as immaterial and incompetent.

The Court: Objection sustained.

Mr. Crittenden: Q. Mr. Hyman advised you as to the community property allegations in the divorce complaint?

Mr. Campbell: Objected to as immaterial and incompetent.

The Court: The objection is sustained.

Mr. Crittenden: Q. Did Mr. Hyman advise you the effect of a default on any allegations in the complaint, or not?

Mr. Campbell: Objected to as immaterial and incompetent.

The Court: The objection is sustained.

Mr. Crittenden: Q. Did Mr. Hyman advise you of the effect of alleging community property if there was default taken or a non-contested matter of this sort, this divorce?

Mr. Campbell: Objected to as immaterial and incompetent.

The Court: The objection is sustained.

Mr. Crittenden: Q. Did Mr. Hyman advise you as to the effect of the allegations that there were community property in the divorce complaint if it were contested?

Mr. Campbell: The same objection, and I ask that the Court instruct counsel to desist from this line. The objections having been theretofore sustained.

The Court: The objection is sustained.

Mr. Crittenden: Do I understand from your Honor that I should not ask any further questions on this? If not, I am not going to waste time here.

The Court: The Court has ruled.

\* \* \* \*—Mrs. O'Connor—(Tr. page 811)

Q. Now, do you know Mr. Tormey sitting back there? A. Yes, I do.

Q. Referring to an evening about 9:30 or 10:00 o'clock—

Mr. Campbell: I can't hear you.

Mr. Crittenden: Q. Referring to an evening at 9:30 or 10:00 o'clock—

Mr. Campbell: May we have the year?

Mr. Crittenden: I am going to try to find that from her.

Q. Do you remember that he came to your bar about 9:30 or 10:00 o'clock one night?

A. Yes, it was in the spring. It was either in February or March of 1946.

Q. When was your attention first called to him?

Mr. Campbell: Objected to as immaterial.

The Court: Objection sustained.

Mr. Crittenden: Q. Did you have occasion to talk to him that evening?

Mr. Campbell: Objected to as immaterial.

The Court: 1946?

Mr. Campbell: Yes, your Honor, that is what she stated.

Mr. Crittenden: This is in the course of the investigation.

The Court: 1946? Objection sustained.

Mr. Crittenden: Q. What time did he leave that particular evening?

Mr. Campbell: Objected to as immaterial.

The Court: Objection sustained.

Mr. Crittenden: Q. What parties were present at the time he left?

Mr. Campbell: Objected to as immaterial.

The Court: Objection sustained.

Mr. Crittenden: What statements did he make to you at the time he left?



Mr. Campbell: Objected to as immaterial.

The Court: Objection sustained. Now you have a record on that line of testimony.

Mr. Crittenden: Q. Now, could you give me the date when you came to the bar and found Mr. O'Connor and Mr. Tormey there?

Mr. Campbell: The date?

Mr. Crittenden: Just the date.

The Witness: The date?

Mr. Crittenden: Q. Yes.

A. It was after the first meeting, because my husband, Mr. O'Connor at the time was with me and that was the first time—

Mr. Campbell: Can we have the year, Mr. Crittenden?

Mr. Crittenden: Q. What was the approximate date, the year and month?

A. It was in 1945. Oh. I am not quite sure. It was after I met him. It had to be after we met him up there.

Q. November or December.

A. Oh, it was in the fall, I believe, of 1945. It was after we met Mr. Tormey. He was not on the first meeting. It was after I had gotten down to the new place and I didn't move there until September 1945, and that is when he was down at the bar in the afternoon.

Q. When you came up to him?

A. And we took him home.

Mr. Campbell: I ask that that last be stricken.

The Court: It may go out.

Mr. Crittenden: Q. At that time, what was

Mr. O'Connor and Mr. Tormey discussing when you came up there?

Mr. Campbell: Objected to as immaterial.

The Court: Objection is sustained.

Mr. Crittenden: Q. What, if anything, did you do after that?

Mr. Campbell: Same objection.

The Court: The objection is sustained.

Mr. Crittenden: Q. What was said subsequently after you left the bar by Mr. Tormey?

Mr. Campbell: Same objection.

The Court: Same ruling.

Mr. Crittenden: Q. What time did you leave Mr. Tormey that evening?

Mr. Campbell: Objected to as immaterial.

The Court: Objection sustained.

Mr. Crittenden: Q. Now, there was a subsequent time that you saw Mr. Tormey down at your bar after that, wasn't there? A. Yes, sir.

Q. What was the date of that?

A. He was there at night.

Q. No, I mean in the afternoon.

A. In the afternoon he called up for an apartment—

Mr. Campbell: I ask that that be stricken. She is asked for a date.

The Court: Let it go out and the jury will disregard it.

Mr. Crittenden: Q. I want to know the date of that incident.

A. It was three days after he was there at night, and that was in February or March of 1946. It

was within the week, because he asked me for an apartment that night.

Mr. Crittenden: No, just a moment.

Mr. Campbell: I ask that that again be stricken, if the Court please.

The Court: Let it go out and let the jury disregard it for any purpose in this case.

Mr. Crittenden: Q. At the time he came who was with him?

Mr. Campbell: Objected to as immaterial.

The Court: Objection sustained.

Mr. Crittenden: Q. What was said by the various parties, Mr. Tormey and the other person?

Mr. Campbell: Objected as immaterial and incompetent.

The Court: Objection sustained.

Mr. Crittenden: Q. How soon did they leave after they first came?

Mr. Campbell: Same objection.

The Court: Objection sustained.

Mr. Crittenden: Q. And which way did they go?

Mr. Campbell: Objected to as immaterial.

The Court: You desist in your further examination of that character.

\* \* \* \*—Mrs. O'Connor—(Tr. page 819)

Q. And how did you have, how did you make the inventory, did you make these yourself?

Mr. Campbell: Objected to as immaterial.

The Court: The objection is sustained.

Mr. Crittenden: All right.

Q. Now, the bar and the bar fixtures, did you

use any of those after the time you moved when the license expired?

Mr. Campbell: Objected to as immaterial.

A. No, sir.

The Court: The objection is sustained.

\* \* \* \*—Mrs. O'Connor—(Tr. page 828)

### Cross Examination

By Mr. Campbell:

Q. I ask you if those were your initials.

A. Those are my initials, but I didn't say it that way.

Mr. Crittenden: If your Honor please, I think we are wasting a lot of time. It wouldn't make one bit of difference if—

The Court: There is nothing before the court.

Mr. Campbell: Q. Now, Mrs. O'Connor—

Mr. Crittenden: I will object to any further discussion on this subject, because it wouldn't make any difference whether it was a gambling loss or not, it would be deductible.

The Court: Overruled. Proceed in this case.

\* \* \* \*—Mrs. O'Connor—(Tr. page 839)

Q. Five cases Y.P.M. whisky?

A. Yes, that is bar. That is old stock. The Schenley is all right.

Mr. Campbell: I will read this off if I may:

"15 cases Calvert's, 7 cases Rewco Rye, 6 cases Belle of Scotland Scotch, 2½ cases—

Just don't interrupt, Mrs. O'Connor, I will read this in a hurry. "2½ cases mixed call Scotch, 30 cases mixed rums, 15 cases S&J brandy, 15 cases



California brandy, 8 cases mixed vermouth, 5 cases mixed cocktails, 10 cases assorted gin, 2 cases sloe gin, 10 cases assorted wines, 1 case creme de menthe, five cases tequilla, 50 cases assorted beers, one case of vodka, 6 bottles Rock 'n Rye, 2 bottles, Cointreau, 1 bottle of creme de cacao, 6 bottles of cordials—2 apricot, 2 blackberry, 2 cherry—3 cases of champagne, pints.”

That is all.

\* \* \* \*—(Tr. page 840)

Redirect Examination

Mr. Crittenden: Q. Reference has been made to YPM Whisky. What type of whisky is that?

A. It was whisky, but it was stuff that had been standing there and finally I gave it away. It was old stuff but I didn't even know—the bottles were all covered with cobwebs and things.

Q. Did you sell it to your customers at the bar?

A. I never opened it at all. It was on the premises and I just wrote it down there, or he wrote it down. I didn't make up that report.

Q. Rewco Rye?           A. Rico Rye.

Mr. Campbell: I am going to object to the materiality of the quality of the whisky. The purchase price and the fact that she had it after having purchased it is the important thing, if the Court please. I object to the question.

The Court: The objection is sustained.

Mr. Crittenden: Q. Could you sell any of this brandy over the bar?           A. No.

Mr. Campbell: That is objected to as immaterial.

The Court: The objection is sustained.

Mr. Crittenden: Q. Did you have calls for any of these cordials?

Mr. Campbell: Objected to as immaterial.

The Court: The objection is sustained.

## DEFENDANT'S PROPOSED INSTRUCTIONS

### Instruction No. 1

Rents from real property of a taxpayer, which are collected by a mortgagee under an assignment of the rents by the mortgagor to the mortgagee, and such rents are applied upon the debt secured by the mortgage, which debt is not a personal liability of the mortgagor enforceable in an action upon the debt, is not income taxable to the taxpayer mortgagor.

Hilpert v. Commissioner, 5 Cir. 151 F. 2d. 929.

Hadley Falls Trust Co. v. U.S., 22 Fed. Supp. 346.

### Instruction No. 2

Under California Law, a purchase money mortgage for the purchase of real property is not an obligation between the mortgagor and the mortgagee upon which an action at law may be brought for the debt for personal liability of the mortgagor, and there is no deficiency judgment possible upon such a purchase money obligation, but the mortgagee may look to his security only and not to any legally enforceable obligation against the mortgagor.

## Instruction No. 3

If you find from the evidence that the defendant owned income real property subject to a purchase money mortgage under the Laws of California, and the defendant assigned the rents and income of the said property to the mortgagee to collect such rents and income and apply the same upon the purchase money mortgage, and such mortgagee did collect such rents and income and apply the same upon the said mortgage obligations, you cannot consider any of such money so received and applied by the mortgagee, as income of the defendant for the purposes of income taxation.

Hilpert v. Comm'r., 5 Cir. 151 Fed. 2d. 929.

Hadley Falls Trust Co. vs. U.S., 22 F. Supp. 346.

CCP 580b.

Stockton Sav. & Loan Bank v. Massanet, 18 Cal. 2d. 200, 114 P2d. 592.

## Instruction No. 4

In any proceeding before a court of the United States where the genuineness of the handwriting of any person may be involved, any admitted or proved handwriting of such person shall be competent evidence as a basis for comparison by witnesses, or by the jury to prove or disprove such genuineness.

28 USCA 638.

## Instruction No. 5

On the "cash basis" of accounting, a taxpayer reports as income money when it is received irrespective of when it is otherwise due or earned, and expenses and disbursements are taken in the accounting period when paid irrespective of the date when the obligations, expense or disbursement was incurred, payable or due. Ordinarily inventories of a taxpayer are no part of the cash basis of accounting, but are under the "hybred" system of accounting. In the absence of a specific request of the Commissioner of Internal Revenue for a taxpayer to change to or adopt a specific system of accounting, the taxpayer is free to adopt and use any system of accounting that fairly and truly reflects his or her income. The law does not impose upon a taxpayer any specific or particular type of system of accounting not that the taxpayer keep his or her books in any particular manner, so long as it fairly represents his or her income.

The Tax Magazine (CCH) Dept. 47 Accounting Methods for Income Tax Purposes By Wm. Margalies, Page 816.

## Instruction No. 6

Gross receipts of the defendant's business in any accounting period are not of themselves taxable income. It is taxable income that is the condition precedent the prosecution must prove by evidence beyond a reasonable doubt, for one cannot attempt to evade or defraud a tax one does not owe or that



is not raised and imposed by a Federal Statute. Gross receipts are but one item going to make up taxable income, for all business transactions are not profitable nor do they always result in taxable income.

### Instruction No. 7

Honest or bona fide belief of the defendant at the time of making her tax returns involved in the indictment that certain items of income were not taxable income or mistaken concepts of law or of accounting or of taxation, however erroneous and however improbable, is a complete defense and negatives the specific wrongful intent required as an element of the offense of which the defendant stands charged. The offense requires a specific wrongful intent to defraud, that is actual knowledge of the existence of the obligations and duty and the wrongful intent to evade it.

Hargrove vs. U.S., 67 Fed. 2d. 820.

### Instruction No. 8

Ordinarily one is presumed to know the law. However, under the offense of which defendant stands indicted, that presumption that one knows the law does not obtain. Under that offense a material element of the offense is that the defendant at the time she is alleged to have done the act knew the existence of the law and did an affirmative wrongful act knowing it was a violation of that specific law, and that the specific affirmative act so done is the act specified in the count of the indict-

ment. Thus ignorance of the law negatives the specific wrongful intent which is a necessary element of the offense. So also is lack of knowledge of the requirement to include taxable income, if any, not included in the return, sufficient to negative the specific wrongful intent which is a necessary element of the offense.

Hargrove v. U.S., 67 Fed. 2d. 820 5 Cir.

#### Instruction No. 9

A taxpayer is not guilty of a felony within the provisions of Section 145b because the taxpayer has a mistaken concept of what is or is not reportable income under the Income Tax Law, or because the taxpayer has a mistaken concept as to what is or is not an allowable deduction under the Income Tax Law, nor because the taxpayer has a mistaken concept of the Income Tax law, however erroneous and however improbable, nor because the taxpayer forgets certain income at the time of making and filing of the income tax return.

Hargrove v. U.S., 67 Fed. 2d. 520 5 Cir.

#### Instruction No. 10

The doctrine of respondeat superior, that an employer or master is responsible for the acts of his or her employee or servant has no application in the criminal law. One may be criminally liable only in case he does that which the law denounces. Criminal intent cannot be imputed to a person through an agent, without the principal's direct

participation. To be guilty of this intent there must be command, direction or consent by the principal to the doing of the very act.

People v. Armentrout, 118 Cal. App. 761 1 P2d. 556.

Paschen v. U.S., 70 Fed. 2d. 491.

Mobile v. U.S., 3 Cir. 284 Fed. 253.

### Instruction No. 11

If you find from the evidence that the acts, if any, of an attempt to evade or defeat the personal income tax were acts of an accountant, agent, servant or employee of the defendant, you must return your verdict for the defendant, for she cannot be held criminally responsible for acts of her accountant, agent, servant or employee unless those acts were done by her positive command, direction or consent. This positive command, direction or consent of the defendant, if any, cannot be presumed, but must be proved by competent evidence adduced at the trial that strikes convictions in your mind beyond a reasonable doubt and to a moral certainty.

### Instruction No. 12

A taxpayer is not criminally responsible for clerical errors of his or her employees, agents, servant or accountant in making a tax return.

Cooper v. U.S., 9 Fed. 2d. 216 8 Cir.

## Instruction No. 13

One may be criminally liable only in case he or she does that which the law denounces. One is not liable criminally for acts of one's servants, employees, agents or account in which one does not command, direct or consent to such acts by one's positive acts with the intention of knowingly doing that which the law denounces, knowing at the time it is denounced by the law.

## Instruction No. 14

You cannot find the defendant guilty of the offenses charged in the indictment if you find she only wilfully failed to make a return including all of her income, and wilfully failed to pay all the tax on that income.

*Spies v. U.S.*, 317 U.S. 492, 87L.Ed. 418.

## Instruction No. 16

Money or property received by a wife from her spouse or from the community property of the spouse upon a separation or divorce of the spouses is not income to the wife. This is true whether it be by express agreement or by judgment of the Court in awarding community property upon a divorce decree.

## Instruction No. 17

Under the California Community Property Law, the respective interests of the husband and the wife in community property during the continu-



ance of the marriage relation are present, existing and equal interests under the management and control of the husband.

C.C.P. 161 a.

Instruction No. 18

The husband has the management and control of the community personal property, with like absolute power of disposition, other than testamentary, as he has of his separate estate; provided however, that he cannot make a gift of such community property or dispose of the same without a valuable consideration or sell, convey or encumber the furniture, furnishings, or fittings of the home, or the clothing or wearing apparel of the wife or minor children that is community, without the written consent of the wife.

C.C. 172.

Instruction No. 19

Earnings of a wife while living with her husband are community property.

Instruction No. 20

Earnings of the defendant while living with her husband from her services are community property and under the same absolute power of disposition, and the same management and control of the husband as any other community property. For the purposes of this case, the earnings of the defendant from her services in the business during the marriage and while she lived with her husband, are

not distinguishable in their management, control and disposition from earnings of the husband from his employment.

### Instruction No. 21

Where separate property is used in a business of one of the spouses, and the principal part of the income is attributable to the personal service of one or both of the spouses, then the portion attributed to personal services are apportioned as a question of fact. Ordinarily 7% per annum would be income on the invested separate property and as such separate property, and the balance of the income of the business and personal services of the spouse would be community property. As an example and illustration, suppose a wife owned a business involving an investment of \$1000 and the principal income was attributed to the services of the wife from the business, then 7% of the \$1000 or \$70.00 per year would be separate property of the wife, and all income of the business would be community property, over that \$70.00 a year.

Lawrence Oliver v. Comm'r., 4 Tax Ct. 684.

Perira v. Perira, 156 Cal. 1, 103 P. 488.

### Instruction No. 22

Where community and separate property have been mingled so as not to permit identity of the portion that is community and the portion that is separate, all of the property is presumed to be community property.

Roches v. Blair, 9 Cir. 32 F. 2, 222.

## Instruction No. 23

Community property is taxable under the Income Tax law, one half to the husband and one half to the wife.

## Instruction No. 24

Property acquired upon credit of the community property, as for example the earnings of the wife while living with her husband, is community property, even though such property is added to or used with separate property of the wife even though the original property to which it was added was originally the separate property of the wife.

## Instruction No. 25

Money obtained by gambling in a friendly game, undertaken as a pastime or entertainment and not as a business, and which gambling is not prohibited by law is not taxable income.

McDermott v. Com., 150 F2 585.

Washburn v. Com., 5 T.C. No. 162.

## Instruction No. 26

Although income from an unlawful business is taxable income, money obtained in a game of chance undertaken solely for amusement and not as a business is not taxable income.

McDermott v. Com., 150 F. 2d 585.

Washburn v. Com., 5 T.C. No. 162.

## Instruction No. 27

Expenses of entertainment reasonably calculated to enhance business done in connection with one's business or occupation, are deductible expenses in arriving at taxable income.

## Instruction No. 28

Living quarters or accommodations furnished an employee in one's business as part of the compensation of employment is a cost of doing business. The expenses of the employer in connection with such living quarters or accommodations are deductible from gross income in arriving at taxable income.

## Instruction No. 29

Where property is used partly in the taxpayer's business and partly for other uses of the taxpayer, then the deductible costs and expenses of such property is in proportion that it is used in the business bears to its other use not attributable to the business. For example, if the taxpayer should use her automobile say for 6,000 miles in a taxable period in connection with her business and 4,000 miles in the same period for other purposes, 60% of the costs of the automobile operation would be attributable to the business and deductible from gross income to arrive at taxable income.

## Instruction No. 30

Property used in the taxpayer's business, but not exhausted or worthless in the accounting per-



iod, is depreciable over its normally anticipated life under such use. You, the jury are the judge of such factual matters, and you are to apply your own judgment according to the evidence to such matters of depreciation and the rate thereof, and you are not bound by any suggested schedule or rates suggested by the government or any of their experts or witnesses.

### Instruction No. 31

If you find from the evidence that the defendant employed an accountant, provided him with the books and records he requested, and relied in good faith upon the tax return prepared by the accountant, the requisite intent under Section 145 (b) is not present and your verdict must be for the defendant.

### Instruction No. 32

The defendant is not charged with the offense of willful failure to pay a tax. That is another and different offense and is no part of the indictment in this case. Even though you should find the defendant willfully failed to pay a tax, however great, you cannot consider this in your deliberation upon the issues of this case.

*Spies v. U. S.* 317 U.S. 492, 87 L.Ed. 418, 63 S.Ct. 364.

### Instruction No. 33

An affirmative willful attempt, as defined in these instructions, is a necessary element in the offense

of which the defendant stands charged. This element of the offense, an affirmative willful attempt, is never presumed. The burden of proving it, if any existed, is upon the prosecution. Unless you find from the evidence adduced at the trial the affirmative willful attempt of the defendant, if any, to do the specific acts charged in the indictment, beyond a reasonable doubt and to a moral certainty, you must return your verdict for the defendant.

#### Instruction No. 34

The difference between willful failure to pay a tax when due which is made a misdemeanor and is not part of the present case or present indictment, and willful attempt to defeat and evade a tax which is made a felony is not easy to detect or define. Both must be willful, and willful is a word of many meanings, often being influenced by its context. It may mean more applied to non-payment of tax than when applied to failure to make a return, or making a false return. Mere voluntary and purposeful as distinguished from accidental omission might meet the test of willfulness. But in view of our traditional aversion to imprisonment for debt, we could not assume the mere knowing and intentional default in payment of a tax where there had been no willful failure to disclose the liability is intended to constitute a criminal offense of any degree. Willfulness in such a case includes some element of evil motive and want of justification in view of all the financial

circumstances of the taxpayer. The difference between the two offenses is found in the affirmative action implied from the term "attempt." The attempt made criminal by this statute 145(b) does not consist of conduct that would culminate in a more serious crime but for some impossibility of completion or interruption or frustration. This is an independent crime, complete in its most serious form when the attempt is completed and nothing more is added to its criminality by success or consummation, as say of attempted murder. Although the attempt succeed in evading tax, there is no criminal offense of any kind, and prosecution can only be for the attempt.

Willful but passive neglect of the statutory duty constitute the lesser offense of which the accused is not charged and is not involved in this proceedings; but to combine it with a willful and positive attempt to evade a tax in any manner or defeat it by any means lifts the offense to the degree of a felony.

By way of illustration and not limitation, we could think affirmative willful attempt may be inferred from conduct such as the keeping of a double set of books, making false entries, or alterations, or false invoices or documents, destruction of books or records, concealment of assets or covering up sources of income, handling one's affairs to avoid making the records usual in transactions of the kind, and any conduct the likely effect of which would be to mislead or to conceal.

*Spies v. U. S.*, 317 U. S. 492, 87 L. Ed. 418,  
63 S. Ct. 364.

## Instruction No. 35

“Willful” as used in the defining of the offense of which the defendant stands charged, is a word of many meanings. This word “willful” means not only “intentional” “knowing”, or “voluntary”, and in addition to the other things covered in other instructions, the word “willful” means an act done with a bad purpose and a thing done without grounds for believing it lawful, and includes as part of its definition evil motive.

U. S. v. Murdock, 290 U. S. 389, 54 S. Ct. 223,  
78 L. Ed. 381.

## Instruction No. 36

“Willful and knowing” as used in the definition of the offense charged in the indictment, includes not only the definitions covered in other portions of these instructions, but it also includes a specific intent to defraud, and a mere willful doing of the acts charged in the indictment is not enough. It requires a specific wrongful intent, that is actual knowledge of the existence of the obligations imposed by law upon a taxpayer to make and include the specific matters alleged to have been omitted from the returns, and the specific wrongful intent to evade it that is the essence of the offense charged.

Hargrove v. U. S., 67 Fed. 2d. 820.

\* \* \* \*



## Instruction No. 38

Unless you find from the evidence adduced at the trial, beyond a reasonable doubt and to a moral certainty, that the defendant did each and every thing charged in the indictment with actual specific knowledge that such affirmative acts, if any, were done with actual knowledge that such affirmative acts were then known by her to be a specific violation of the tax law of which she stands charged, you must return your verdict for the defendant.

Hargrove v. U. S., 67 Fed. 2d, 820 5 Cir.

## Instruction No. 39

Specific intent to defraud is a necessary element of the offense charged in the indictment. Fraud is never presumed, but the burden of proving it is always upon the prosecution. Each and every element of the intent to defraud must be proved by evidence adduced at the trial, to a moral certainty and beyond a reasonable doubt.

## Instruction No. 40

“Fraud” is a legal term having a specific meaning at law separate and apart from its meaning in common parlance. It involves a number of necessary elements, all of which must concur to constitute “fraud” in its legal sense. “Fraud” as used in its legal sense involves a material representation (2) that the material representation is false (3) scien-ter, that is knowledge by the person making the material false representation that such representa-

tion was false (4) intent that the person to whom the false material representation was made should act upon it in the manner reasonably contemplated (5) that the person to whom the false material representation was made was ignorant of the falsity (6) that the person to whom the false material representation was made relied upon the truth of the said representation (7) that such person relying thereon had a right to rely thereon in the exercise of due diligence under the circumstances (8) that there was injury or damage the consequent and proximate cause of such acts and reliance. No part of fraud as the term is used in the law is ever presumed, but must be proved by competent evidence adduced at the trial that strikes conviction in the minds of the jury beyond a reasonable doubt and to a moral certainty. Failure to prove each and every element of the fraud by such evidence must result in a finding by the jury that there was no fraud.

26 C. A. 1062.

\* \* \* \*

#### Instruction No. 42

If you find from the evidence that the defendant discovered after she made and filed any of the returns involved in this case that any income had been omitted therefrom or that such return was incorrect in any manner, you cannot consider such omission or incorrect statement or discovery or the failure to discover in your deliberations, for

none of these are any element of the offense of which the defendant stands charged.

Guzik v. U. S., 54 F. 2d., 618 cert. den. 285 U. S. 545.

### Instruction No. 43

You must find from the evidence adduced at the trial, beyond a reasonable doubt and to a moral certainty, that the defendant owed, and the Federal Statutes raised and imposed a tax charged in the indictment counts for there to be an offense, even if all of the other elements of the offense are found from the evidence beyond a reasonable doubt and to a moral certainty to be present. No one can attempt to evade and defraud a tax which is not raised and imposed by the Federal Statute and owed by him or her. Defendant's liability for the said taxes, if any, is a condition precedent to a commission of the offense charged in the indictment. The defendant's liability for the said taxes, if any, is not the essence of the offense, except as one of the necessary elements which the prosecution must prove by evidence adduced at the trial beyond a reasonable doubt and to a moral certainty.

### Instruction No. 44

In determining whether the defendant is liable for the tax, if any, alleged in the indictment, which is a condition precedent to alleged offense, for one cannot attempt to evade and defraud a tax one does not owe; you must consider only the evidence

adduced at the trial and properly admitted by the Court. Arguments of counsel are no part of this proof. No part of the alleged liability is presumed. The burden of proving not only the gross income of the defendant, if any, during the periods of time covered in the indictment, but also all proper deductions to arrive at the proper tax liability, if any, is upon the prosecution. No part of the burden of proof of any of the elements necessary to prove proper tax liability if any, is upon the defendant. This burden of proof never shifts. The quantum of proof of this alleged tax liability of the defendant is not that of civil cases which is a mere preponderance, nor does the determination by any governmental agency raise any presumption as in matters before the Internal Revenue Department or in civil litigation, but each and every element to make up the alleged liability of the defendant must be proved with the same quantum of proof as other elements in a criminal case, which the prosecution must prove.

#### Instruction No. 45

In making and filing an income tax return a taxpayer need only report such income as he or she believes is taxable income and the taxpayer may take all deductions in such return as he or she may believe proper. In doing so, the taxpayer is not acting at his or her peril of prosecution under Section 145(b), if the law or the Internal Revenue Bureau should determine there was other income reportable or taxable, or some or all of



the deductions claimed by the taxpayer are not proper. The reported decisions of the United States Courts are full of reported judicial decisions where the taxpayer and the Bureau of Internal Revenue differed as to what was or what was not taxable income and as to what was and what was not proper deductions. The United States Courts, can and on some occasions do, construe the tax laws differently than the Bureau of Internal Revenue has by its published regulations. On the other hand, the Bureau of Internal Revenue does not always acquiesce in the decisions of the United States Courts even when final; and the Bureau continues to apply the tax laws without regard to the judicial decisions in which it does not acquiesce. Congress has provided for determination of such disputes by an adequate system of procedure, including assessments and judicial reviews in such civil matters. Whether or not **there has been any assessment** or civil proceedings between the taxpayer and the Bureau of Internal Revenue, is no issue in this criminal trial. The outcome of this criminal proceedings in no way effects nor concerns such civil liability, if any, or the assessment or collection of any tax, if any, of the defendant.

#### Instruction No. 46

When a taxpayer entertains a doubt as to what income or money is reportable or what items are deductible expenses, the taxpayer in making and filing his or her return is free to resolve all such doubts in his or her favor. This is true even though

there may be some regulation of the Bureau of Internal Revenue which the taxpayer may believe is not in accord with a law of Congress or of the United States Constitution. This is true even though the taxpayer is ignorant of some law or judicial decision among the reported cases. It is not the intention of Congress to punish as a felony under Section 145(b), any such acts of a taxpayer.

Instruction No. 47

The applicable statutes provide that losses incurred in trade or business or losses incurred in transactions entered into for profit, though not connected with trade or business, and losses of property not connected with trade or business arising from casualty or theft are deductible from gross income.

1945 Master Tax Guide U. S., see 306 Code Section 23(e).

Instruction No. 48

The applicable statutes specifically designate bad debts as deductions in computing net income.

1945 Master Guide U. S., see Code Section 23(k).

Instruction No. 49

In lieu of the deduction for specific debts actually worthless, there may be deducted a reasonable reserve for bad debts, at the option of the taxpayer.

Reg. Sec. 29.23(k)—1 (2).

## Instruction No. 50

The Defendant in filing a joint return with her husband in 1942 did not thereby lose any of her rights or her identity as an individual separate taxpayer for that accounting period.

*Cole v. Connors*, 9 Cir. 81 F. 2, 485.

## Instruction No. 51

You are not to take into your consideration, in deliberation upon the evidence as to income of the defendant for the year 1942, any income of her then husband, Mr. Jost. The filing of a joint return imposes joint liability only as to the amount of tax, if any, shown due by the joint return. The filing of a joint return does not surrender the spouses' individuality as a separate taxpayer; but the duty is upon the prosecution to prove beyond a reasonable doubt the defendant's individual tax liability, if any, from competent evidence adduced and admitted at the trial. No part of the defendant's husband's vested interest in one half of the community property is income of the defendant.

*Cole v. Connors*, 9 Cir. 81 F. 2, 485.

## Instruction No. 52

You are instructed that under the first count of the indictment, the Defendant is charged solely with attempting to defeat and evade income tax for the calendar year, 1942. As to the year 1942 if you find that the tax imposed upon the defendant for the taxable year 1942 was not greater than the

tax for the taxable year 1943 and you further find that the Defendant has not been convicted of any criminal offense with respect to the tax for the taxable year 1942 and that no tax assessment has been made by the United States Treasury Department against the defendant for the taxable year 1942, then I instruct you that it is the law that the liability of the defendant for the tax imposed for the taxable year 1942 was discharged on September 1, 1943.

Sec. 6, Current Tax Payment Act of 1943.

Instruction No. 53

You are instructed that the Current Tax Payment Act of 1943 placed the Defendant upon a current basis for taxable years beginning after December 31, 1942 and relieved the Defendant from paying two years tax liabilities in one year. The general effect of this provision was to cut down the amount of tax liability otherwise payable by the defendant 100% of the tax liability for the lower of the years 1942 or 1943. Thus if you find the tax liability of the defendant for the taxable year 1942 to be lower than the tax liability for the taxable year 1943, then the entire tax liability for the taxable year 1942 is discharged as of September 1, 1943, but the tax imposed by the Internal Revenue Code for the taxable year beginning in 1943 is increased.

Sec. 6, Current Tax Payment Act of 1943.



## Instruction No. 54

As to the divorce action between the defendant and William B. Jost, the jury is instructed that if they find that the defendant, (Catherine O'Connor), obtained the decree of divorce therein by default of the defendant, William B. Jost, then it is the law of the State of California that such judgment becomes in effect a contract between the parties thereto; then any community property not disposed of in such judgment of divorce continued after the judgment to be held by the parties as tenants in common.

Brown v. Brown, 170 Cal. 1, 174 Pac. 1168.

Loraine v. Loraine, 8 Cal. App. (2) 687 48  
Pac. (2) 48.

## Instruction No. 55

The jury is instructed that if they find that in the divorce action between the defendant and William B. Jost there was never an award of any community property to either spouse in either the interlocutory or final decree then if there were any community property in existence at the date of the final decree of divorce, such property remained the property of both spouses thereafter and they continued to hold the same as tenants in common after the date of the final decree of divorce therein.

Brown v. Brown, 170 Cal. 1, 174 Pac. 1168.

Loraine v. Loraine, 8 Cal. App. (2) 687, 48  
Pac. (2) 48.

## Instruction No. 56

The jury is instructed that if they find that in the divorce action against William B. Jost that the Plaintiff in her complaint claimed all of the property of the parties as her own, and that the plaintiff further thereafter obtained a default judgment of divorce against William B. Jost, then the jury is instructed that it is the law in the State of California that such judgment became in effect a contract between the parties thereto whereunder all community property interest of the defendant, William B. Jost, passed to the plaintiff as her sole and separate property.

Brown v. Brown, 170 Cal. 1, 174 Pac. 1168.

Loraine v. Loraine, 8 Cal. App (2) 687 48 Pac.  
(2) 48.

## Instruction No. 57

The presumption that all criminal acts of a wife are done in the presence of the husband by his coercion arises even if the wife at the time of such acts is not within the view of her husband. It is sufficient that she is in the same proximity as her husband, that is, in the same building.

30 C. J., 792.

## Instruction No. 58

If you find that any of the elements of the offense charged in the indictment were done by the defendant in the presence of her spouse, you must

presume such acts or omissions were done at the coercion of the husband.

30 C. J., 792.

Instruction No. 59

The presumption that all criminal acts of a wife done in the presence of her husband are done under his coercion is a species of evidence that persists throughout the trial and during your deliberation unless and until overcome by positive evidence, if any, adduced at the trial that strikes conviction in your minds beyond a reasonable doubt and to a moral certainty to the contrary.

30 C. J., 792.

Instruction No. 60

All criminal acts of a wife done in the presence of her husband are presumed to be done at the coercion of her husband, and she cannot be held criminally for acts done by coercion and not by her criminal intent.

30 C. J., 791.

Instruction No. 61

You are directed to return your verdict of not guilty upon the first count of the indictment (covering the taxable year 1942).

Instruction No. 62

You are directed to return your verdict of not guilty upon the second count of the indictment (taxable year 1943).

## Instruction No. 63

You are directed to return your verdict of not guilty upon the third count of the indictment (taxable year 1944).

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Tuesday, April 6, 1948

10:00 o'clock a.m.

(After the cause was argued by respective counsel, and at the conclusion thereof, the Court charged the jury as follows:)

The Court: It now becomes the duty of the Court to instruct the jury on the law of this case, and it becomes the duty of the jury to apply the law thus given to them to the facts before them; the jury are the sole judges of the facts.

It is the duty of the jury to give uniform consideration to all of the instructions herein given, to consider the whole and every part thereof together and to accept such instructions as a correct statement of the law involved.

The defendant in this case is charged with a violation of a certain federal law which has to do with the payment of income tax to the United States. It is known as Section 145(b) of the Internal Revenue Code. Among other things it provides that any person who wilfully attempts in any manner to evade or defeat any tax imposed by this chapter or the payment therefor, shall, in addition to other penalties provided by law, be guilty of a felony, and upon conviction therefor shall be punished as the statute provides.



The defendant in this case, accordingly, has been charged with a violation of that particular law. The indictment is in three counts; that is, there are three separate charges, the first of which charges the violation of this law, in that the defendant in 1943 wilfully attempted to defeat and evade a large part of income tax owing by her to the United States for the year 1942 by filing and causing to be filed a false and fraudulent income tax return, whereas it is charged in this indictment she incorrectly stated and falsely stated her net income for the year 1942, stating it to be substantially less than as the indictment charges it was. A similar offense is charged in the second count of the indictment for the calendar year 1943, and a similar offense is charged in the third count of the indictment for the calendar year 1944. Therefore the jury has three separate problems to consider; whether there was a violation of the statute for the defendant in the calendar year 1942, and also for the year 1943, and also for the year 1944.

There are a few matters of law that pertain to the criminal liability under this statute, which I will give you as simply and concisely as I can. The gravamen—that is, the gist of the law—is that if a taxpayer does some affirmative act wilfully in an attempt to evade or avoid an income tax imposed, or the collection thereof, he is guilty of a felony. There must be upon the part of the taxpayer, in order that he may be convicted or found guilty, a wilful affirmative act or acts of some kind whose purpose it is to avoid or defeat the tax itself or

the collection of the tax. Even the filing of an incorrect or false income tax return of itself is not a felony unless it may be said that you may find that it be a conscious, wilful, affirmative act performed by the defendant for the purpose of either evading the tax itself, or evading the payment of it. The offense with which the defendant is charged in this case requires a specific wrongful attempt to defeat the United States in the collection or imposition of the tax. There must be on the part of the defendant actual knowledge of the existence of her obligation to pay this tax, and to report it, and a wrongful attempt to avoid that duty and responsibility.

The fact that an indictment has been filed against the defendant is not to be considered by you as any evidence of the defendant's guilt. The indictment is merely a legal accusation charging a defendant with the commission of a crime. It is not, however, evidence any such defendant and does not create any presumption or inference of the defendant's guilt, and you are not to consider such fact in arriving at your verdict.

The federal government levies a tax on the net income of every individual. The applicable statutes define "net income" as gross income less deductions authorized by law.

"Gross income" includes gains, profits and income derived from salaries, wages, or compensation for personal service of whatever kind and in whatever form paid, also professions, vocations, trades, businesses, commerce or sales or dealings in property, whether real or personal, growing out of the

ownership, or use of, or interest in, such property; also from interest, rentals, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

The applicable statutes provide that the following expenses are deductible from gross income in order to compute net income for income tax purposes:

1. The ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business; such ordinary and necessary expenses may include reasonable expenses of entertainment necessarily done in connection with one's business or occupation for the purpose of enhancing the value of the business;

2. Interest paid or incurred during the taxable year on indebtedness;

3. Taxes paid or incurred during the taxable year except Federal income taxes;

4. Depreciation—defined as a reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, or of property held for the production of income;

5. Charitable contributions—which means contributions made by the taxpayer to a charitable organization for its use in carrying out its purposes.

In 1944, the applicable statutes allowed the taxpayer to deduct \$500 if her gross income less business expenses was over \$5,000, instead of deducting charitable contributions, interest and other non-business expenses.

You have been instructed that ordinary and necessary business expenditures are deductible from gross income. You should understand, however, that all business expenditures are not deductible, even though they be ordinary and necessary.

Those business expenditures which are made for the purchase of what is known as "capital assets" are not deductible. Specifically, if the expenditure is for the purchase of something which is not ordinarily used up in a year, it is not deductible. For example, an expenditure for the purchase of furniture for a rooming house or a bar is not deductible as an ordinary or necessary business expense; while money spent to purchase whiskey or food to be sold at a bar is so deductible.

You are instructed that gifts to individuals, however needy or deserving they may be, are not deductible as charitable contributions. Only contributions to an organized charity, such as the Red Cross, are deductible in computing income taxes.

Before the income tax on net income is computed, the applicable statutes allow certain "personal exemptions" to be deducted, depending on the marital status of the taxpayer.

For 1942 the statutes allowed a taxpayer who was married and living with his or her husband or wife a personal exemption of \$1,200. Only one such exemption was allowed for each couple living together. If a joint return was filed by the husband and the wife, the whole exemption could be taken on that return.

For 1943 the statutes allowed a personal exemp-



tion in the same amount. If the spouses were living together for part of the year, the taxpayer was entitled to deduct only that proportional part of the exemption for married taxpayers. The statutes also allowed a personal exemption of \$1,200 for a taxpayer who was not married, or married and not living with her husband or wife, if he or she was the head of a family.

For 1944 the applicable statutes allowed a personal exemption of \$500 to be deducted by each taxpayer who was not married and not the head of a family, or married but not living with his or her husband or wife.

You are instructed that the earnings of the defendant while she was living apart from her husband, William Jost, were her separate income and were not in any way community income, or income to William Jost, either before or after the commencement or termination of divorce proceedings.

The Government has offered proof that defendant owned a half interest in the bar known as Kay's Club before she married William Jost, that she purchased the other half interest with money she borrowed, that no assets of William Jost's were vested in Kay's Club, and that defendant was the sole proprietor and manager of Kay's Club. The Government has also offered proof that William Jost laid no claim to any part of the income from Kay's Club, and that defendant purported to report all the income from Kay's Club on her separate income tax returns for 1943 and 1944, and that defendant stated, under oath, that there was no community property between herself and William Jost.

If you believe the Government's evidence, you may find from these facts that William Jost relinquished any claim he might have had to defendant's earnings from Kay's Club, or any claim that the income from Kay's Club was community income. You are instructed that such relinquishment by William Jost had the effect of making the income from Kay's Club the separate income of defendant.

The defendant is charged with having violated the Internal Revenue laws by having wilfully attempted to evade and defeat part of the income taxes due from her with respect to 1942, 1943 and 1944. To prove this charge for any year, the Government must prove, together with other elements which I will define later, that the defendant did some act in that year which tended to conceal her true tax liability from the Government.

It is the law that any act, of whatever kind, which tends to evade taxes is enough to make up this crime. Among the acts which are sufficient in making the Government's case are: keeping false books, filing false returns, destruction of books and records, and the concealment of assets. This list is not complete, but is merely a list of examples of the kind of acts which Congress intended to punish.

The Government must not only prove that defendant did some act which tended to conceal her true tax liability, but must also prove that this act was done wilfully.

"Wilful" in the statute which makes a wilful attempt to evade taxes a crime, refers to the state of

mind in which the act of evasion was done. It includes several states of mind, any one of which may be the wilfulness necessary to make up the crime. Wilfulness includes doing an act with a bad purpose. It includes doing an act without a justifiable excuse. It includes doing an act without ground for believing that the act is lawful, and it also includes doing an act with careless disregard or whether or not one has the right to so act.

You are instructed that it is not necessary for the Government to offer direct proof of wilfulness. It is a rare case in which the defendant has said to a witness that he did certain acts with the purpose of evading his tax liabilities.

In making your decision, therefore, as to whether or not the acts tending to conceal defendant's true tax liability are wilful, you may consider all the circumstances of the case. You may infer wilfulness from any kind of evasion, if any, which you find defendant committed, from her opportunity to know the true amount of her net income and from such other facts which point to the existence or non-existence of the criminal state of mind in the defendant.

The Government has offered proof in this case that defendant was the sole proprietor of Kay's Club, and was the person who managed and directed its affairs. You are instructed that you may infer from this fact that defendant knew the true amount of gross income which was taken in by Kay's Club.

Besides proving the commission of acts tending

to conceal defendant's true tax liability and proving that these acts were wilfully done by defendant, the Government must also prove that defendant owed more income tax than she reported as due.

The indictment alleges that defendant owed a certain amount of tax and reported as due a smaller amount in each of the three years with which this trial was concerned. The Government, however, need not prove that defendant owed the exact amount of tax alleged in the indictment. It is sufficient proof of the Government's case as to any year if you find that the defendant owed any substantial amount of tax for that year in addition to the amount reported as due.

As part of the proof of its case, the Government has offered evidence that defendant had more gross income and net income in each year than she reported on her returns for that year. As proof of the true amount of the defendant's gross and net income, the Government has offered evidence that defendant deposited certain amounts of money in her bank accounts in each year, and that she spent certain other amounts of money which, if you believe the Government's evidence, were not deposited in any bank, and so are not counted in totalling up her bank deposits.

You are instructed that proof that a person has a business from which she derives income, together with proof that that person makes frequent deposits to a bank account, and proof that she draws on that bank account for her own use, is potent proof that deposits to her bank account made in any



year are made from her gross income earned in that year.

You are further instructed that proof that a person who had such a source of income spent a certain amount of money in a particular year is proof that that money came from the person's gross income for that year.

Ordinarily one is presumed to know the law. However, with respect to the crime with which this defendant is charged, namely, wilfully attempting to evade and defeat her income tax liability by filing a false return, you are instructed you may not find her guilty on any of the three counts unless you find that she knew that the law required her to file true and correct income tax returns.

If you find from the evidence that the defendant employed an accountant, provided him with truthful books and records and fully disclosed to him all her gross income and her true deductible expenditures, and if you further find that having done all of this, she relied on good faith on his advise, you are instructed that the wilfulness which is a requisite of this offense is not present here.

You are instructed that where a husband and wife file a joint return, and where later a deficiency in tax is asserted, the spouse on whose additional income the deficiency is asserted is liable for the deficiency in tax. Thus if you find in this case that the income or any part of it which was not reported in 1942 was the income of the defendant, you are instructed that she is severally liable for the income tax on that unreported income.

You are instructed that if you believe the defendant wilfully attempted to evade and defeat a substantial part of her 1942 tax liability by filing a false return for that year, you should find her guilty on the first count, despite the forgiveness features of the applicable tax statutes, since the tax law forgave taxes for 1942 or 1943 only where there was no fraud only on the part of the taxpayer in reporting them.

Gifts from whatever source, even from a husband, are no part of income chargeable to the donee of the gift. Gifts are taxable under a separate statute and their returns and taxation are no concern of the jury or of the issues of this case.

The specific wrongful intent with actual knowledge of the act being a violation of the statutory duty of the taxpayer that is an essential element of the offense charged is never presumed. The burden of proving it is always upon the prosecution. This element of offense must be proved by evidence adduced at the trial that strikes conviction in your mind beyond a reasonable doubt and to a moral certainty.

The defendant stands charged with only the offenses set forth in the various counts of the indictment. She is not charged with any other offense or offenses. Unless each and every element of the offense charged is proved by competent evidence adduced at the trial beyond a reasonable doubt and to a moral certainty, you must return your verdict of acquittal. Even if the evidence should justify your finding that the defendant has committed some

other offense, you are to wholly disregard such other offense in arriving at your verdict.

The applicable statutes specifically designate bad debts as deductions in computing net income.

There has been some mention in the testimony of income of the defendant from gambling. In so far as that may be material to a determination of a specific issue as to whether or not there was, during the three years in question, a wilful and fraudulent attempt by the defendant to evade the payment or the imposition of an income tax by the United States, let me say that the tax statute makes no difference between income obtained from illegal or from legal activities. All sorts of income are taxable in the same manner. Net income from gambling is taxable like any other income. As far as the collection of taxes is concerned, the Government is not interested in how or where a man earns money. It is only interested in his paying a tax on that which represents his net earnings.

The determination of a charge in a criminal case involves the proof of two distinct propositions: first, that the crime charged was committed; and second, that it was committed by the person accused thereof and on trial therefor. These two propositions and every essential and material fact necessary to them or to either of them must be established by the Government to a moral certainty and beyond a reasonable doubt.

Every person charged with crime is presumed to be innocent, and this presumption has the effect of evidence and continues to operate on his behalf

until it is overcome by competent evidence. It is not necessary for the defendant to prove her innocence; the burden rests upon the prosecution to establish every element of the crime charged, to a moral certainty and beyond a reasonable doubt.

A reasonable doubt is such a doubt as you may have in your minds when, after fairly and impartially considering all of the evidence, you do not feel satisfied to a moral certainty of the defendant's guilt. In order that the evidence submitted shall afford proof beyond a reasonable doubt, it must be such as you would be willing to act upon in the most important and vital matters relating to your own affairs. Reasonable doubt is not a mere possible or imaginary doubt, or a bare conjecture; for it is difficult to prove a thing to an absolute certainty.

You are to consider the strong probabilities of the case. A conviction is justified only when such probabilities exclude all reasonable doubt as the same has been defined to you. Without it being restated or repeated, you are to understand that the requirement that a defendant's guilt be shown beyond a reasonable doubt is to be considered in connection with and as accompanying all the instructions that are given to you.

There are two classes of evidence recognized and admitted in courts of justice, upon either of which juries may lawfully find an accused guilty of crime. One is direct or positive testimony of an eyewitness to the commission of the crime, and the other is proof by testimony of a chain of circumstances pointing sufficiently strong to the commission of the



crime by a defendant, and which is known as circumstantial evidence. Such evidence may consist of admissions by the defendant, plans laid for the commission of the crime, such as putting himself in position to commit it—in short, any acts, declarations or circumstances admitted in evidence tending to connect the defendant with the commission of the crime.

Circumstantial evidence includes any fact which may tend to prove the issues presented, and may consist of any act, circumstances or declaration admitted in evidence and tending to connect the defendant with the commission of the crime charged. In order to convict, the circumstances must be such as to produce the same degree of certainty as direct evidence. There is nothing in the nature of circumstantial evidence which renders it any less reliable than any other class of evidence; if it produces in the minds of the jury a conclusion of the defendant's guilt beyond all reasonable doubt, it is sufficient.

If, upon consideration of the whole cause, you are satisfied to a moral certainty and beyond a reasonable doubt of the guilt of the defendant, you should so find, irrespective of whether such certainty has been produced by direct evidence or by circumstantial evidence. The law makes no distinction between circumstantial and direct evidence in the degree of proof required for conviction, but only requires the jury shall be satisfied beyond a reasonable doubt by evidence of either the one character or the other, or both.

In every crime there must exist a union or joint operation of act and intent; and for a conviction, both elements must be proven to a moral certainty and beyond a reasonable doubt. Such intent is merely the purpose or willingness to commit such acts. It does not also require a knowledge that such act is a violation of law.

However, a person must be presumed to intend to do that which he voluntarily or wilfully does in fact do, and must also be presumed to intend all the natural, probably and usual consequences of his own acts.

The Court further instructs the jury that the intent or intention with which an act is done is manifest by the circumstances connected with the offense and the sound mind and discretion of the accused. All persons are of sound mind who are neither idiots nor lunatics nor affected with insanity.

You, the jury, are the sole judges of the credibility and the weight which is to be given to the different witnesses who have testified upon this trial. The witness is presumed to speak the truth. This presumption, however, may be repelled by the manner in which he testifies, by the character of his testimony, or by evidence affecting his character for truth, honesty and integrity, or his motives; or by contradicting evidence. In judging the credibility of the witnesses in this case, you may believe the whole or any part of the evidence of any witness, or may disbelieve the part of it as may be dictated by your judgment as reasonable jurors.

You should carefully scrutinize the testimony given, and in so doing, consider all of the circumstances under which any witness has testified, his demeanor, his manner while on the stand, his intelligence, the relations which he bears to the Government or the defendant, if at all, and every matter that tends reasonably to shed light upon his credibility. If a witness is shown knowingly to have testified falsely on the trial touching any material matter, the jury should distrust his testimony in other particulars and in that case you are at liberty to reject the whole of the witness' testimony.

In determining the credibility of a witness, you should consider whether the testimony of any witness is in itself contradictory, whether it has been contradicted by other credible witnesses, whether the statement made by any witnesses are reasonable or unreasonable, whether they are consistent with other statements or with the facts established by other evidence or admitted facts.

You may also consider the witness' manner of testifying on examination, the character of the testimony, the bias or prejudice, if any, manifested, the interest or absence of interest in the case, their degree of intelligence, their recollection—whether good or bad, clear or indistinct, concerning the facts testified to, the inclination or motives together with the opportunity of the witness knowing the facts whereof he may speak.

A witness may be impeached by the party against whom he was called by contradictory evidence, by evidence that he has made at other times statements

inconsistent with his present testimony. If you find that any witness has been impeached or that the presumption of truthfulness attached to the testimony of such witness has been repelled, then you will give the testimony of such witness such credibility, if any, as you may consider it entitled to. Where a showing of inconsistent statements by way of impeachment is allowed and made, you as jurors nevertheless remain the exclusive judges of the credibility of all the witnesses, and are just as much entitled to believe the witness whose statements are impeached as the witness who impeached.

You have been confronted with what the law calls "expert testimony." The difference between ordinary and expert testimony is as follows:

Ordinarily a witness is allowed to testify only as to facts which he has seen or observed. An exception to this rule occurs in the case of a so-called "expert witness", who is allowed to give his opinion in any matter pertaining to a science, art or trade in which he is skilled. The amount of skill, training or study devoted by the particular expert to the field in which he gives his opinion goes to the weight of his evidence and must be determined by you.

If you should find that a particular expert witness possesses the necessary background, training and experience in the subject matter involved in his discussion, then you shall consider his opinion as a matter of evidence which shall be treated in the same light as any facts testified to in the case.

Duly qualified experts have given their opinions



on questions in controversy at this trial. To assist you in deciding such questions, you may consider the opinion with the reasons stated therefor, if any, by the expert who gives the opinion. You are bound to accept the opinion of an expert as conclusive, but you should give to it the weight to which you shall find it to be entitled. You may disregard any such opinion if you find it to be unreasonable.

You are instructed that while the defendant in a criminal action is not required to take the stand and testify, yet if he or she does so, her credibility and the value and effect of her evidence are to be weighed and determined by the same rules as the credibility and effect and value of the evidence of any other witness to be determined. If a defendant elects to take the stand and testify in her own behalf, her testimony is to be weighed in the same manner and measured according to the same standard as the testimony of any other witness, and the tests for determining credibility of witnesses as given you in another part of the instructions are to be applied to her testimony alike with that of all other witnesses. No greater or lesser presumption attaches in favor of her testimony than attaches to that of any other witness—with this additional feature, however: that you should weigh the defendant's testimony in the light of the fact that she is the defendant in the case, and that she has an interest in the outcome of the case because of that fact.

The Court cautions you to distinguish carefully

between the facts testified to by the witnesses and the statements made by the attorneys in their arguments, or presentations as to what facts have been or are to be proved. And if there is a variance between the two, you must, in arriving at your verdict—to the extent that there is such variance—consider only the facts testified to by the witnesses. And you are to remember that statements of counsel in their arguments or presentations are not evidence in the case. If counsel, upon either side, have made any statements in your presence concerning the facts of the case, you must be careful not to regard such statements as evidence and must look entirely to the proof in ascertaining what the facts are.

If counsel, however, have stipulated or agreed to certain facts, you are to regard the facts so stipulated to as being conclusively proven.

The court charges you that evidence admitted for a limited purpose is to be considered by the jury for such purpose, and none other. Under this rule it is the duty of the jury, when the propositions are facts to which such evidence is addressed and determined, to exclude such evidence in its consideration of all other matters of fact in the case.

It sometimes happens during the trial of the case that objections are made to questions asked or to offers made to prove certain facts, which objections are sustained by the Court; and it sometimes happens that evidence given by a witness is stricken out by the Court on motion. In any of such cases, you are instructed that in arriving at a verdict you

are not to consider as evidence anything that has been stricken out by the Court or anything offered to be proven or contained in any question to which an objection has been sustained by the Court.

If counsel on either side, or the Court, during the pendency of this proceeding, made any statement outside of the record—that is, a statement which was not pertinent or relative or material to the issues involved in this case, or if the Court in discussing with counsel any objection or motion made any statement which seemed to you to reflect upon counsel or seemed to you to indicate that the Court had some opinion upon the merits of the case or upon some fact or issues involved in the case, then the Court admonishes you to disregard any such statement, if such statement was made, in reaching a verdict in this case.

If you should find that there are discrepancies or inconsistencies existing in the testimony of any witness or between the testimony of any witnesses, or if you should find yourselves disagreeing over various issues, real or apparent, you should then ascertain whether or not such discrepancies or inconsistencies, or such points of difference, affect the true issues in this case. Examine such discrepancies or inconsistencies and such disputed points; look at the same squarely and ask yourselves these questions: How does the decision of this or that or the other discrepancy or matter in dispute affect the guilt or innocence of the defendant? Regardless of what may be the truth concerning such discrepancies or inconsistencies,

ask yourselves the main question: Did or did not the defendant commit the crime as alleged in the indictment? Is such discrepancy or such disputed point material to establish the main or material issue of fact as to the guilt or innocence of the defendant? If they are not material, if the decision of the same is not necessary to enable you to arrive at the truth of the guilt or innocence of the defendant, then such discrepancies or disputed points are immaterial and minor matters, and do not waste any further time discussing or considering them. Spend no time in the discussion of minor matters which, whether true or false, do not affect and are not necessary to enable you to answer the important question: Did the defendant do those things set forth in the allegations of the indictment?

Although as men and women, you may sympathize with those who suffer, yet as honest men and women, bound by oath to administer judgment according to law and evidence, you should not act upon your sympathies without any proof. Mercy does not belong to you. No question of mercy, sentiment or anything else resides in you, except the question of whether or not you believe, from the evidence, and beyond a reasonable doubt, that the defendant is guilty. You should return your verdict accordingly.

If you are aware of the penalty prescribed by law, it is your duty to disregard that knowledge. In other words, your sole duty is to decide whether the defendant is guilty or not guilty of what she is



charged with. The question of punishment is left wholly to the Court, except as the law circumscribes its power.

There is nothing peculiarly different in the way a jury is to consider the proof in a criminal case from that by which jurors given their attention to any question depending upon evidence presented to them. You are expected to use your good sense, consider the evidence for the purposes only for which it has been admitted, and in the light of your knowledge of the natural tendencies and propensities of human beings, resolve the facts according to deliberate and cautious judgment; and while remembering that a defendant is entitled to any reasonable doubt that may remain in your minds, remember as well that if no such doubt remains, the Government is entitled to a verdict.

In determining what your verdict shall be, you are to consider only the evidence before you. Any testimony as to which an objection was sustained, and any testimony which was ordered stricken out, must be wholly left out of account in this case.

The verdict of the jury should represent the opinion of each individual juror; it by no means follows that the opinions may not be changed in the juryroom. The very object of the jury system is to secure unanimity by a comparison of views and by arguments among the jurors themselves.

Jurors are expected to agree upon a verdict where they can conscientiously do so. You are expected to consult with one another in a juryroom, and any juror should not hesitate to abandon his own view when convinced that it is erroneous.

Your verdict must be unanimous.

When you retire to your juryroom to deliberate, you must select one of your number as foreman, and he will sign your verdict for you when it has been agreed upon, and he will represent you as spokesman in the further conduct of this case in this court.

The Clerk has prepared a form of verdict for you; you will take it to the juryroom with you. The form of the verdict is made out in blank and reads as follows:

“We, the jury, find the defendant at the bar as follows: ..... as to the first count, ..... as to the second count, and ..... as to the third count.”

When you have agreed upon this verdict, you will fill in those three blanks and you will have your foreman sign it and return it into court.

I think that covers all of the matters. The jury will now retire and deliberate upon their verdict.

No. 11,911

IN THE

United States Court of Appeals  
For the Ninth Circuit

CATHERINE O'CONNOR,

*Appellant,*

VS.

UNITED STATES OF AMERICA,

*Appellee.*

On Appeal from the District Court of the United States  
for the Northern District of California.

BRIEF FOR THE UNITED STATES.

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FILED

1979

PAUL P. O'BRIEN





## Subject Index

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	Page
Opinion below .....	1
Jurisdiction .....	1
Statement of questions involved .....	2
Statutes involved .....	3
Statement .....	4
Argument:	
I. The appellant was not prejudiced by refusal of court to grant further particulars .....	9
II. The evidence is more than ample to support the verdict .....	12
III. No prejudicial errors occurred by reason of the ad- mission or exclusion of evidence and the appellant was accorded a fair trial .....	13
IV. No error occurred in the instructions given by the court to the jury, or in the rejection of any of ap- pellant's proposed instructions .....	18
Conclusion .....	26

## Table of Authorities Cited

<b>Cases</b>	<b>Pages</b>
Brown v. Brown, 170 Cal. 1, 174 Pac. 1168 .....	14
Cole v. Commissioner, 81 F. 2d 485 .....	14
Conyer v. United States, 80 F. 2d 292, 294 .....	23
Dawson v. United States, 10 F. 2d 106, certiorari denied, 46 S. Ct. 638, 271 U. S. 687 .....	23
Hill v. United States, 298 U. S. 460, 56 S. Ct. 760.....	26
Hilpert v. Commissioner, 151 F. 2d 929 .....	19
Lorraine v. Lorraine, 8 Cal. App. 2d 887, 48 P. 2d 48.....	14
Maxfield v. United States, 152 F. 2d 593, 596, certiorari denied, 327 U. S. 794, 66 S. Ct. 821, 90 L. Ed. 1021....	9, 10, 12
Ng Sing v. United States, 8 F. 2d 919, 920 .....	16
Robinson v. United States, 33 F. 2d 238, 240 .....	9
Spies v. United States, 317 U. S. 492, 63 S. Ct. 364.....	25
United States v. Murdock, 290 U. S. 389, 54 S. Ct. 223....	25
Ward v. Commissioner, 58 F. 2d 757 .....	19
Wong Tai v. United States, 273 U. S. 77, 82, 47 S. Ct. 300, 71 L. Ed. 545 .....	9

### Statutes

Current Tax Payment Act of 1943, The, Sec. 6(a).....	22
Internal Revenue Code, Sec. 22(d)(1) .....	20
Internal Revenue Code, Sec. 145(b) (26 U.S.C. 145(b))....	1, 2, 3

### Miscellaneous

Federal Rules of Criminal Procedure, Rule 30 .....	24
Treasury Regulations 111, Sec. 29.22(c)-1 .....	20

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**BRIEF FOR THE UNITED STATES.**

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**OPINION BELOW.**

The court rendered no opinion.

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**JURISDICTION.**

The appellant, Catherine O'Connor, was indicted on July 9, 1947, in the District Court for the Northern District of California, Southern Division, as follows:

Count One—for wilfully and knowingly attempting to evade and defeat her personal income taxes in the amount of \$1,103.46, for the calendar year 1942, in violation of Section 145(b), Internal Revenue Code;

Count Two—for wilfully and knowingly attempting to evade and defeat \$6,630.90 of her personal income and Victory taxes for the calendar year 1943, in violation of Section 145(b), Internal Revenue Code;

Count Three—for wilfully and knowingly attempting to evade and defeat \$8,967.48 of her personal income taxes for the calendar year 1944, in violation of Section 145(b), Internal Revenue Code. (R. 1-5.)

Motion for bill of particulars and motion to dismiss indictment were denied on September 22, 1947, and the defendant entered a plea of not guilty to each count of the indictment. (R. 33-34.) Trial was had in the District Court and on April 6, 1948, jury returned a verdict finding appellant guilty on the first count of the indictment and stated they were unable to agree on the second and third counts of the indictment. (R. 35.) On April 21, 1948, the District Court committed appellant to the custody of the Attorney General for imprisonment for a period of six months and to pay a fine in the sum of \$5,000.00 on the first count of the indictment. (R. 38-41.) Notice of Appeal was filed on April 22, 1948. (R. 42-43.)

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#### STATEMENT OF QUESTIONS INVOLVED.

1. Did any prejudice occur by reason of the Court having denied appellant's request for a bill of particulars containing greater detail than that furnished by the Government?



The Government contends that no prejudice occurred, and further, even if it be considered that the denial of further particulars was in the first instance erroneous, appellant was not taken by surprise in any particular or prejudiced in any matter at a second trial of the same issues, at which the same witnesses were called.

2. Is the evidence sufficient to support the verdict?

The Government contends that the evidence is more than ample to support the verdict.

3. Did prejudicial errors occur during the trial?

The Government contends that no prejudicial errors occurred, and that appellant was given a fair trial.

4. Did prejudicial error occur in the instructions given by the Court to the jury, or in the rejection of any of appellant's proposed instructions?

The Government contends that the instructions were full and complete, fairly and clearly stated the law with reference to the issues, and that no prejudice resulted from the denial of any of appellant's proposed instructions.

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#### STATUTES INVOLVED.

Title 26, Internal Revenue Code:

##### SEC. 145. PENALTIES.

\* \* \* \* \*

(b) Any person required under this title to collect, account for, and pay over any tax im-

posed by this title, who willfully fails to collect or truthfully account for and pay over such tax, and any person who willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof, shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, be fined not more than \$10,000, or imprisoned for not more than five years, or both, together with the costs of prosecution.

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#### STATEMENT.

Appellant has not seen fit to make a statement of the evidence, except as appears incidentally in the course of the argument in her brief. Moreover, such statements of evidence as do appear are incomplete, fragmentary, and in many instances either contrary to the record or entirely unsupported by it. For this reason, it is deemed proper to make a statement of the evidence for the assistance of this Honorable Court.

The appellant, Catherine O'Connor, who is occasionally referred to in the testimony by the names of Catherine Larson and Catherine Jost (names of previous husbands), was engaged in the tavern or bar business in the city of San Francisco, California, during the entire period covered by the indictment. From January 1, 1942, until July 15, 1942, the business was operated as a copartnership with one Victor Divers,

each partner having an equal interest. (R. 120-122.)<sup>1</sup> As of July 15, 1942, Divers sold his one-half interest in the business to appellant for \$1,600.00. (Ex. 13; R. 123, 124.) During the course of the partnership a gray bound ledger was maintained, purporting to show the daily receipts and disbursements of the partnership business. (Ex. 14; R. 124, 125.) Entries were made in this book by each partner. (R. 126.) At the time the partnership was severed this record was left on the business premises. (R. 125.) Appellant, as sole proprietor of the business, continued to enter the daily receipts of the business in this book to and including August 23, 1942. (Ex. 14; R. 156-182; 205-217.)

In the course of a routine examination of appellant's income tax returns for the years 1942, 1943 and 1944 by a deputy collector, made as a result of an anonymous letter (R. 84), appellant was asked to produce the records of her business. She then produced a ledger or daybook (Ex. 5), containing entries purporting to show receipts and disbursements of the business for the period July 16, 1942, to December 31, 1944, and stated that the entries in it were made by herself. (R. 87.) This book was supplied to the accountant who prepared her returns, and was his sole source of information as to receipts and disbursements

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<sup>1</sup>Page numbers of the Transcript of Record as used herein are those set forth on official Transcript of Record certified to by the Clerk of the District Court, and appear in the transcript by the use of a numbering machine. It is noted, however, that appellant has used court reporter's numbers so that the numbers used by appellant are approximately 79 page numbers away from the official number.

for the period July 16, 1942, to December 31, 1944 (R. 280-282), with the exception of certain rentals received by appellant in 1944 (R. 282, 283). The accountant relied upon Exhibit 5 as correctly setting forth the receipts of the tavern business. (R. 283.)

Although appellant denied under oath the entries of receipts made in the "gray book" (Ex. 14) for the period July 16, 1942, to August 23, 1942, were in her handwriting, she admitted that certain of the disbursements listed during that period were in her handwriting and others in the handwriting of her then husband, William Jost. (R. 141-145; Ex. 15.) An attempt had been made to obliterate the figures in the receipts column of the "gray book" for the period July 16 to August 23, 1942, by ink and pencil scrawlings. (Ex. 14; R. 147.) Similar obliterations were observed on check stubs of the appellant by the examining agent. (R. 148.) These check stubs were returned to the appellant on July 8, 1946, and her receipt therefor obtained. (R. 149; Ex. 16.) They were not produced during the trial.

Two competent and qualified examiners of questioned documents, E. O. Heinrich (R. 91-205), and Postal Inspector James E. Conway (R. 205-220), pronounced the figures of receipts in the "gray book" (Ex. 14) for the period July 16 to August 23, 1942, as being definitely in appellant's handwriting. The receipts figures in the "gray book" averaged in excess of \$17.00 per day more than the daily receipts figures in Exhibit 5. (R. 384-385.)



Unable to rely upon receipts figures in Exhibit 5, the Government agents analyzed appellant's income by three methods. These were (1) application of funds (R. 385-390); (2) annual increases in net worth (R. 390); (3) applying average daily understatement of \$17.00 per day to the entire period after appellant acquired full title to the business. (R. 391.) Each of these methods produced comparable figures:

Net income r return filed	Net income method #1	Net income method #2	Net income method #3
\$ 777.29 (Ex. 2)	\$ 3,788.52 (Ex. 28)	\$ 5,176.39 (Ex. 31)	\$ 3,837.29 (R. 391)
7,879.28 (Ex. 3)	17,612.82 (Ex. 29)	13,536.86 (Ex. 31)	13,999.28 (R. 391)
5,091.98 (Ex. 4)	11,110.42 (Ex. 30)	10,688.33 (Ex. 31)	11,211.98 (R. 391)
<hr/> 13,748.55	<hr/> \$32,511.76	<hr/> \$29,401.58	<hr/> \$29,048.55

During the period in question the appellant purchased and completely paid for an apartment house at a cost of \$17,000.00, an amount in excess of her total reported income, without regard to other assets acquired and necessary living expenses. (Ex. 31.)

Appellant called to the stand Special Agent Paul Tormey, who testified that he had made an audit of her income for the years 1942, 1943 and 1944. His testimony was that he had found the correct income as compared to the returns filed, as follows (R. 710, 711):

<u>Year</u>	<u>Per Return</u>	<u>Per Audit</u>
1942	\$ 777.29	\$ 4,840.73
1943	7,879.28	19,472.00
1944	5,091.98	22,552.30

Tormey reconciled the higher income figures of his audit with those of Krause, by stating that the differ-

ence arose from Krause having allowed appellant every item of deduction which she had claimed either in her returns or in her testimony at the previous trial, whether or not the items could be substantiated or were ordinarily allowable. (R. 711-712.) Special Agent Clarence Krause stated that his instructions were "to lean over backwards . . . on any items whatsoever where there would be any doubt at all about it, anything Mrs. O'Connor claimed, give her the benefit of the doubt and allow it, which is exactly what was done in this case." (R. 508.)

In addition to daily receipts, false entries were made by appellant in Exhibit 5 with reference to charitable donations. In each of the years a number of items purporting to be donations to the Red Cross, Salvation Army, and other charities were included on the books and a substantial part thereof claimed as deductions on the returns. (R. 368-370.) After attempted verification, appellant was questioned under oath on November 1, 1943, at which time she stated that such payments were to police officers. (R. 470-1, Ex. 33.) Subsequently, she claimed that such payments were in fact to cover gambling losses (R. 371), and so testified at the trial (R. 896-7).

**ARGUMENT.****I.****THE APPELLANT WAS NOT PREJUDICED BY REFUSAL OF COURT TO GRANT FURTHER PARTICULARS.**

On July 31, 1947, appellant filed a Demand for Bill of Particulars. (R. 6-9.) On the same date, the Government filed an answer, furnishing certain of the matters requested, but stating as to others that appellant was in possession of ascertaining such facts. (R. 10-14.) Thereafter, on August 26, 1947, appellant filed a document entitled Motion for Bill of Particulars or In the Alternative To Make Indictment More Certain, supported by certain affidavits. (R. 15-26.) Thereafter, the Court denied the latter motions. (R. 31.)

Appellant now apparently complains that the ruling of the Court was prejudicial to the preparation of her case to the extent that she was taken by surprise by the testimony regarding accounting computations by the Government at the trial, and further by her inability to make exhaustive examinations of the worksheets of the accountant at times when the Court was not in session. (Op. Br. 25-51.)

It is well settled that the granting or denial of a bill of particulars is in the sound discretion of the trial court, and if no abuse or prejudice appears its action in denying the application will not be disturbed on appeal. *Wong Tai v. United States*, 273 U.S. 77, 82, 47 S. Ct. 300, 71 L. Ed. 545; *Robinson v. United States*, 9 Cir., 33 F. 2d 238, 240; *Maxfield v. United*

*States*, 9 Cir., 152 F. 2d 593, 596, cert. den., 327 U.S. 794, 66 S. Ct. 821, 90 L. Ed. 1021.

In the case of *Maxfield v. United States*, *supra*, this Court states:

. . . The indictments clearly informed appellants of the annual amount of income on account of which taxes were allegedly evaded; and the figures given were intelligibly broken down. Appellants had their records in their own possession and were in position to analyze the general allegations of the bill. There was no showing or appearance of surprise, nor was any continuance requested while the trial was in progress.

The situation in the instant case is exactly analogous. The indictment (R. 1-5) clearly sets forth the source of appellant's income, and the nature of her deductions. It states the amounts of tax sought to be evaded. Appellant had her records in her own possession since July 8, 1946, when they were returned by the agents and a receipt given by appellant therefor (Ex. 16), with the exception of the "gray book" Exhibit 14, which was made available to appellant at all times (R. 27-28), a fact not denied by appellant's counsel (R. 30), until introduced in evidence at the first trial. Thereafter it remained in the custody of the District Court Clerk, until introduced in evidence at the second trial.

If any surprise could have existed on the part of appellant with respect to the evidence of the Government, it was dissipated by the fact of a first trial involving the same issues and the same witnesses,



with the exception of two handwriting experts called by the Government. Indeed, the only surprise apparently claimed by appellant is the fact that the Government caused a new audit to be made between the first and second trial for the purpose of resolving every conceivable doubt in favor of appellant. (R. 508, 711-12, 419.)

Appellant further complains that the refusal for further particulars resulted in prejudice to her case in that demands to see work-sheets of the witness Krause were not acceded to. However, on direct examination, this witness did not testify directly from such sheets, but from schedules prepared from appellant's books and records, and schedules agreed upon with appellant and her counsel, all of which were placed in evidence. (Exhs. 23, 24, 25, 26, R. 357-419.) Counsel for appellant minutely cross-examined Krause on the items going to make up his audit. (R. 450-485.) While the witness was on the stand, he offered the detailed schedules to counsel, but they were declined. (R. 484-485.)

Examination of the portions of the Record referred to by appellant indicate that the requests for the work-sheets were for their examination outside the sessions of Court, or that they be placed in evidence as Government exhibits. The Government refused to accede to the latter request, as the thousands of items involved would have but further encumbered the record, and they were nothing but recapitulations of matters already in evidence.

In his argument, counsel for appellant states (Op. Br. 38):

This is a trial where an agent testifies that he has investigated the defendant and finds her guilty.

*No such testimony is in the record.*

---

## II.

### THE EVIDENCE IS MORE THAN AMPLE TO SUPPORT THE VERDICT.

In her Opening Brief, pages 4 to 24, appellant argues principally to the contention that the evidence was insufficient to support the verdict. A short statement of the evidence set out at the opening of this brief under the heading Statement of Facts clearly indicates that the evidence was more than sufficient to justify the verdict.

The evidence clearly shows that the appellant understated her income for each year in question. As to wilfulness and the intent to evade tax, it was shown that she made false entries in her books understating her true income, and made false entries relative to charitable donations. The false records were supplied by her to the witness Bosserman from which to prepare her returns. During the investigation she made false statements concerning her true income and as to the authenticity of certain of her records. It was not necessary for the Government to prove the exact amounts of unreported income as alleged in the indictment, nor to offer direct proof of wilfulness and intent. *Maxfield v. United States, supra.*

## III.

**NO PREJUDICIAL ERRORS OCCURRED BY REASON OF THE  
ADMISSION OR EXCLUSION OF EVIDENCE AND THE AP-  
PELLANT WAS ACCORDED A FAIR TRIAL.**

In her Opening Brief, pages 51 to 57, appellant complains of rulings of the court by which it is claimed that much admissible evidence was excluded. Throughout the brief, appellant claims that she was not afforded a fair trial.

**(A) ADMISSION AND EXCLUSIONS OF EVIDENCE.**

Most of the objections to the exclusion of evidence fall of their own weight, as the evidence was clearly inadmissible, and in any event its exclusion would not constitute prejudicial error.

(1) At pages 51 and 55 to 57, Appellant's Opening Brief, she complains as to the Court's rulings with respect to a community property issue sought to be injected into the case by her. The evidence showed that appellant and one William Jost were married in March, 1942, separated on July 8, 1943, that appellant received an interlocutory decree of divorce on July 22, 1943 (R. 230-231) and a final decree of divorce one year later (R. 116-117). The complaint in the divorce proceeding, to which the default of Jost was entered, recited, over the verification of appellant, that there was no community property the result of the marriage and that all the property of the appellant was her separate property. (R. 113-115.) The interlocutory and final decrees were silent as to community property. (R. 113-115.)

The courts of California have determined that in such a state of the pleadings, the final decree of divorce, although silent as to property, nevertheless operates as an adjudication that at the time the action was begun there was no community property. *Brown v. Brown*, 170 Cal. 1, 174 Pac. 1168; *Lorraine v. Lorraine*, 8 Cal. App. (2d) 887, 48 Pac. (2d) 48.

The evidence shows that at all times the appellant exercised complete management and direction of the tavern, and that the husband received no part of the income or assets of the business, either during or after marriage. (R. 231-232.) The money to purchase the one-half interest in the business from Divers was borrowed by appellant under the name of Catherine Larson, and on her own credit. (R. 107-108.) The bank accounts were also carried in the name of Catherine Larson. (R. 104-105, Ex. 8), (R. 110-111, Ex. 10.)

The conviction which is here appealed relates only to the calendar year 1942. For that year, appellant and her then husband chose to file a joint return (Ex. 2), purporting to return all of the taxable income of both spouses, from whatever source. Each is therefore liable for any deficiency from his or her separate income. *Cole v. Commissioner*, 81 F. 2d 485.

(2) Appellant asserts (Op. Br. 51-52) that she was precluded from impeaching the veracity of a bartender formerly employed by her by inquiring into the number and amount of drinks of liquor he had each day. *The question was permitted by the Court,*



*was answered by the witness, and the subject explored in detail. (R. 274-275.)*

(3) Appellant asserts (Op. Br. 52-53) that the cross-examination of the witness Shannon as to opening amounts in the cash register each day was not permitted. The record is contrary to such assertion, as the questions asked by appellant's counsel, with the exception of one which assumed a fact not in evidence, were permitted to be asked and answered by the witness. (R. 271-272.)

(4) Appellant objects to the Court having sustained objections to certain questions asked the witness Bosserman during cross-examination on the grounds that if the answers were permitted, they would have impeached this witness. (Op. Br. 53-55.) Examination of the Record, pages 318 to 328, discloses that as to many of these questions, counsel did not lay the proper foundation as to impeachment, and as to others that he mislead the witness as to contents of the record on the first trial.

(5) Appellant asserts (Op. Br. 59) misconduct on the part of Government counsel for interposing an objection to a question during the cross-examination of the witness Washauer on the ground that the question was argumentative and misstated the record (R. 101-102). Appellant's attorney stated that the objection was an attempt by Government counsel "to get his witness out of a difficult position." (R. 102.) It was this latter statement that the Court referred to as "unwarranted" and ordered the jury to disregard it,

on objection of the Government. It is submitted that counsel's characterization of Government's objection was gratuitous and uncalled for. However, the Court's statement cannot be properly termed a reprimand or, if so, it cannot be considered uncalled for.

**(B) APPELLANT WAS ACCORDED A FAIR TRIAL.**

Throughout their brief, and consuming a large portion of it, counsel for appellant have seen fit to launch a bitter, vituperative, at times scurrilous and at all times wholly unwarranted attack upon the motives, honesty and character of practically everyone having any connection with the trial. These include the agents who made the investigation, the officials of the Bureau of Internal Revenue who reviewed the evidence, those of the Department of Justice who approved it for prosecution, the Grand Jury which returned the indictment, the officials of the Government who presented the case to the trial jury, and finally even the Trial Judge. Counsel have referred to the trial as being one by "denunciation", a term, incidentally, which they employ some twenty-one times in their brief. (Op. Br. 19-39.) The term "denunciation" is an apt description of Appellant's Opening Brief.

Counsel assert (Op. Br. 13-14) that it was improper for the Trial Judge to rule that a motion for dismissal upon the grounds of insufficiency of the evidence should be made in the presence of the jury. It has long been settled in this Circuit that this is a matter wholly in the discretion of the judge. *Ng Sing v.*

*United States*, 8 F. 2d 919, 920. In excusing their failure to renew the motion before the jury, counsel assert they considered their "very low percent of success . . . on motions and ruling . . . upon matters that appeared meritorious." They likened the manner of the Court in his rulings to that of a "drill sergeant to a recruit" and other rulings "spoken with inflection implied defense counsel had no valid point and was 'bamboozling' the court." Therefore, they concluded, that if the Court ruled on the motion to dismiss, it "might well be said with such inflections and intonations of the Court as to amount to a directed verdict to convict."

Again, counsel state the Trial Judge threatened them with contempt. (Op. Br. 16-17.) Examination of the record discloses that no such threat was made.

The Judge, after sustaining objections to a certain line of questions, ordered counsel to desist from further questions of the same nature. When counsel failed to do so, the Court warned him to obey the order of the Court. The questions in issue were in an attempt to impeach his own witness, and objection was properly sustained. (R. 605-608.)

A further direct attack is made upon the Trial Judge on pages 24-25, Appellant's Opening Brief. There he is charged with sustaining Government objections "no matter how weak or illfounded." By inference, at least, the Judge is accused of being a party to a "trial by denunciation," and making "due process, the requirement of an indictment by a grand

jury, etc. . . . but empty phrases in the Constitution.”  
(Cf. App. Op. Br. 38-39.)

“The eminent fairness, judicial attainments, and universal courtesy to all parties appearing before him of the District Judge thus unfairly attacked is too well known to the Bench and Bar to dignify such charges by answer. Suffice it to say that the assertions of counsel for appellant can be supported *neither on nor off the record*. Counsel for the Government feel, however, that these and similar absolutely unsupported attacks upon the Court and our judicial system, by members of the Bar of this Honorable Court should be called to its attention. For support, counsel for appellant do not even attempt to cite the record in the majority of instances.

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#### IV.

#### NO ERROR OCCURRED IN THE INSTRUCTIONS GIVEN BY THE COURT TO THE JURY, OR IN THE REJECTION OF ANY OF APPELLANT'S PROPOSED INSTRUCTIONS.

Appellant complains that the Court committed error in refusing numerous instructions to the jury requested by her, and that certain of the instructions given by the Court constituted reversible error. (Op. Br. 60-80.) These matters will be treated in the same order as referred to in the Opening Brief.

(1) Appellant's proposed instructions 1, 2, and 3 (R. 46-47) are predicated on the theory that rents from real property are not income to the mortgagor-



owner of the property if the rents have been assigned to the mortgagee to be applied against the purchase price of the property in California where a deficiency judgment cannot be obtained upon default of a purchase-money obligation. This is not a correct statement of the law.

This Court has held that where the holder of a leasehold interest merely assigns rentals without assigning lease itself, assigned rentals were property taxed as income of assignor. *Ward v. Commissioner*, 58 F. 2d 757. The case of *Hilpert v. Commissioner*, 151 F. 2d 929, relied upon by appellant (Op. Br. 60-61) has no pertinency. There, the question involved whether or not certain rents were taxable to one person, when in fact they accrued entirely to the benefit of another, and when the first person had made a purported sale of the property and reported the gain realized thereby. In the instant case, the net rentals accrued entirely to the taxpayer by way of increasing her equity in the property, and, ultimately (and in the period here in question) resulting in her obtaining clear title to it.

(2) Appellant complains (Op. Br. 61) that the Court did not give an instruction with regard to expert testimony in the language of the statute (28 U.S.C. 638) as in proposed instruction No. 4 (R. 47). The instruction given, however (R. 934), was full and complete. All of the documents in question, together with the admitted or proven handwriting, was before the jury in the course of the trial and in their deliber-

ations. They were instructed that they were not bound to accept the opinions of the experts.<sup>2</sup>

(3) Proposed Instruction Number 5 (R. 47-48), discussed by appellant (Op. Br. 61) is not a correct statement of the law in that it implies that appellant was under no obligation to report inventory changes on her income tax returns.

Whatever the system of accounting used by a taxpayer, inventory changes must be reported "when- ever, in the opinion of the Commissioner, the use of inventories is necessary in order clearly to determine the income of any taxpayer. . . ." *Internal Revenue Code Section 22(d)(1)*. By *Regulations 111, Sec. 29.22(c)-1*, the Commissioner requires that inventory change must be reported "in every case in which the production, purchase, or sale of merchandise is an income-producing factor."

(4) Appellant's Proposed Instruction No. 6 (R. 48) was fully covered in the Court's instructions (R. 919-921) wherein full and complete instructions were given as to the meanings of gross and net income, deductible business expenses, etc. Despite appellant's assertion to the contrary (Op. Br. 61), the law with relation to burden of proof was covered by the Court (R. 927-8).

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<sup>2</sup>A typographical error appears in the Court's instructions at line 21, page 934, of the Record on Appeal. The sentence as given by the Court commenced: "You are *not* bound to accept the opinion of an expert as conclusive. . . ." (Emphasis supplied.)

(5) Proposed instructions 7, 8 and 9 (R. 49-50) are fully covered by the Court in his instruction, so far as pertinent (R. 918-919, 924, 925, 926).

(6) Appellant's Proposed Instructions Nos. 10, 11, 12, and 13 (R. 50-52) deal with the liability of a principal for the acts of his agent. It has no application to the instant case. The only matters with relation to appellant's business which were not performed personally by her, was the placing of the figures in the returns by the accountant Bosserman. His testimony was that the partnership return (Exh. 1), covering the period January 1 to July 15, 1942, was prepared from the "gray book" (Exh. 14), and that the balance of the returns (Exhs. 2, 3, 4) were prepared from Exhibit 5, with the exception of rental income for 1944, which was supplied by appellant (R. 278-283). No other records were supplied to him. (R. 281.) He relied upon the receipts as set forth in Exhibit 5 as being accurate. (R. 283.) His employment was only to prepare the returns, and no audit was made by him. (R. 278.) Under this state of the record, the Court properly instructed the jury relative to her reliance on the accountant. (R. 926.)

(7) Proposed Instructions Nos. 14, 32, 33, and 34 (R. 52, 58-59) are not applicable to the present charge. The appellant was not charged with wilful failure to file (indeed, the evidence showed returns filed for each year), nor with wilful failure to pay. The Court instructed clearly as to the nature of the charge, the elements which the Government must prove to sustain the charge, and, finally, that the jury should disre-

gard any other offense which the evidence might indicate. (R. 928.) The proposed instructions would have served but to confuse the jury as to the real issues.

(8) Appellant offered a number of instructions relative to community property which are referred to in Appellant's Opening Brief, pages 64 to 67. The matter of community property rights have heretofore been treated in this brief. The evidence clearly shows that the omitted income was that of the wife. The false return, resulting in the understatement and attempted evasion of a substantial amount of the tax owed on the joint incomes of the husband and wife were caused entirely by her acts, and not through any acts of the husband. The proposed instructions were properly rejected.

(9) Appellant's Proposed Instructions Nos. 52 and 53 (R. 68-69) are clearly not applicable. *The Current Tax Payment Act of 1943*, Public No. 68-78th Congress, H.R. 2570, in Section 6(a), relative to forgiveness of 1942 income taxes under certain situations, makes the following proviso:

. . . This subsection shall not apply in any case in which the taxpayer is convicted of any criminal offense with respect to the tax for the taxable year 1942 or in which additional tax for such taxable year are applicable by reason of fraud.

Obviously, if the jury found from the evidence that appellant attempted wilfully to evade and defeat a substantial part of her 1942 tax liability by filing a false return for that year, the Current Tax Payment



Act would have no application. The Court so instructed the jury. (R. 927.)

(10) Appellant offered proposed instructions Nos. 57, 58, and 59 (R. 71-72) attempting to raise a presumption that criminal acts performed by a wife in the presence of her husband are presumed to be at the coercion of the husband. (Op. Br. 74-75). While such a legal fiction existed at common law, it is no longer valid in the light of modern day conditions, where the participation of women in the business world on an equal basis with men, requires that they assume their full responsibility in regard to criminal acts, in the absence of a positive showing that such acts were due to the coercion of the husband. This view is expressed in *Conyer v. United States*, 80 F. 2d 292, 294 (C.C.A. 6th) wherein the Court states:

The modern statutes dealing with the status of women have modified the common-law rule that a woman violating a statute in the presence of her husband is presumed to be acting under his coercion. The independence of women in political, social, and economic matters rightly places upon them an increased responsibility. We find no reversible error in the refusal of the Court to charge as requested upon this point.

The evidence in this case has shown that appellant was the active moving party in the offense committed; indeed, that her husband did not participate in any manner. The Court did not err in failing to give the proposed instructions. Cf. *Dawson v. United States*, 10 F. 2d 106 (C.C.A. 9th) certiorari denied, 46 S.Ct. 638, 271 U.S. 687.

(11) The balance of the instructions requested by appellant and refused by the Court were either without application, or were fully and adequately covered by the instructions given.

(12) Appellant has found fault with certain of the instructions given by the Court. (Op. Br. 75-80.) However, no exceptions were taken by appellant to the charge as given by the Court. *Rule 30, Federal Rules of Criminal Procedure*, provides in part:

. . . No party may assign as error any portion of the charge or omission therefrom unless he objects thereto before the jury retires to consider its verdict, stating distinctly the matter to which he objects and the grounds of his objection. . . .

Clearly, appellant can not raise the issue for the first time at this point.

In their argument with respect to the instructions as given, counsel for appellant have misquoted or misconstrued many of the instructions given, without calling the attention of this Honorable Court to where in the Record on Appeal the alleged improper instructions occur, or giving effect to the instructions as a whole. Only by reading instructions as a whole can it be seen how one instruction is enlarged, modified, or explained by another.

Counsel frequently accuse the Court of giving "formula" instructions on various matters. We confess we are unable to understand this term as applied to instructions, nor the implication of counsel in using it.

For example, counsel state (Op. Br. 75) that the Court gave a formula instruction amounting to a direction to the jury to disregard community property. It is presumed that counsel are referring to the instruction appearing at pages 922 and 923 of the Record on Appeal. The instruction was merely to the effect that if the jury chose to believe certain of the evidence offered by the Government it could arrive at certain conclusions therefrom. There is no direction to the jury that they must do so.

Counsel refer to purchase of a half interest (presumably in the tavern) on the credit of the community. (Op. Br. 75.) Nowhere in the record is there evidence that the credit of the community was so utilized. On the contrary, the evidence showed that the money to purchase the half-interest from Divers was secured from the Morris Plan Company, from whom appellant had borrowed money prior to her marriage to Jost, and was borrowed under the name of Catherine Larson. (R. 107-108.) Nowhere does the name of Jost appear in the transaction.

The Court's instructions on what acts would constitute a violation of the statute were taken directly from *Spies v. United States*, 317 U.S. 492, 63 S. Ct. 364; those relative to wilfulness from *United States v. Murdock*, 290 U.S. 389, 54 S. Ct. 223. Both are recognized as the leading cases on their subject matter.

**CONCLUSION.**

It is respectfully submitted that appellant was not prejudiced by any of the rulings of the Trial Court or by its instructions given or refused. A reading of the entire record and of the exhibits submitted conclusively demonstrate her guilt. She was given a trial which was eminently fair in every respect. The sentence and judgment of the Court are in exact conformance. (R. 38-41.) Cf. *Hill v. United States*, 298 U.S. 460, 56 S. Ct. 760.

The conviction should be affirmed.

Dated, January 31, 1949.

Respectfully submitted,

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No. 11,911

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IN THE

United States Court of Appeals  
for the Ninth Circuit

CATHERINE O'CONNOR,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

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APPELLANT'S REPLY BRIEF

FILED

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MAR 5 1949

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## Table of Contents

	PAGE
I. It Is Proper for Counsel for a Defendant in a Criminal Matter to Urge the Client's Constitutional Rights and Assign Error Before the Above-entitled Court.....	1
II. Computations Based Upon Investigation of Third Person's Books Not in Evidence; and Computations Not Subject to Determination as to the Various Items Nor Subject to Inspection Do Not Meet the Requirements of Fair Play.....	4
III. The Prosecution's Attempted Explanation of the Discrepancies Between Their First Trial Computations and Their Second Trial Computations Does Not Explain the Greater Increase in "Corrected Business Receipts" Charged in the Second Trial Computations .....	5
IV. The Prosecution Proved the Authenticity of the "Gray Book" by Comparisons with the Mysterious Check Stubs by Alleged Obliterations Not Before the Jury.....	6
V. Naming of Deductions Which Statute Permits a Taxpayer to Take by Either Name is Made a "Red Herring" to Prejudice the Accused .....	6
VI. The Exceptions Were Properly Made the Subject of Exceptions by the Defendant Before the Jury Retired.....	8
VII. The Same Disclosure Was Made to Defendant's Accountant Bosserman as Was Alleged to Be Proof of Falsity During the Trial. Having Made a Full Disclosure, She Had a Right to Rely Upon the Professional Skill and Services of Her Accountant .....	9

	PAGE
VIII. The Failure to Provide the Bill of Particulars Resulted in Serious Prejudice and Surprise.....	12
IX. The Laws of California as to Community Property Are Necessary for the Determination of the Income of the De- fendant .....	15
Conclusions .....	18



## Statutes and Textbooks

	PAGE
<i>Black's Law Dictionary</i> , (2nd Ed.), p. 354.....	14
<i>Bouvier's Law Dictionary</i> (Banks Ed.), p. 292.....	14
<i>Civil Code</i> , 161a, 164 .....	15

## Table of Authorities

<i>Chandler v. Chandler</i> , 112 Cal. App. 601, 297 p. 636.....	16
<i>Crossan v. Crossan</i> , 35 Cal. App. 2d 39, 94 p. (2d) 609.....	16
<i>Estate of Fellows</i> , 106 Cal. App. 681, 289 p. 887.....	16
<i>Falk v. Falk</i> , 48 Cal. App. 2d. 762, 120 p. (2d) 715.....	16
<i>Henry v. Hibernia Sav. &amp; Loan Soc.</i> , 5 Cal. App. 2d 141, 42 p. (2d) 395 .....	16
<i>Martin v. Southern Pac. Co.</i> , 130 Cal. 285, 62 p. 515.....	16
<i>McCarthy's Estate</i> , in re, 127 Cal. App. 80, 15 p. (2d) 223.....	16
<i>Mosesian v. Parker</i> , 44 Cal. App. 2d 544, 112 p. (2d) 705.....	15
<i>Moulton v. Moulton</i> , 182 Cal. 185, 187 p. 421.....	15
<i>Lawrence Oliver v. Comm'r.</i> , 4 Tax Court 684.....	16
<i>Periera v. Periera</i> , 156 Cal. 1, 103, p. 488.....	16
<i>Provost v. Provost</i> , 102 Cal. App. 775, 283 p. 842.....	16



No. 11,911

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IN THE

United States Court of Appeals  
for the Ninth Circuit

CATHERINE O'CONNOR,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

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**APPELLANT'S REPLY BRIEF**

---

To the Honorable Above-Entitled Court:

I.

**It Is Proper for Counsel for a Defendant in a Criminal Matter to Urge the Client's Constitutional Rights and Assign Error Before the Above-Entitled Court.**

The United States Government's brief in this case characterizes Appellant's Brief as a "denunciation" (Pg. 16) and the appeal for the client's Constitutional rights and discussion of error as "bitter," "vituperative," "at times scurrilous" and "at all times wholly unwarranted" (Pg. 16). Counsel for the defense have undertaken to discharge their duty as counsel and officers of this court as fearlessly and as ably as they could, in good faith as they see these vital matters presented in the record.

Canons of Profesisonal Ethics, American Bar Association, provides Canon No. 5 "... Having undertaken such defense (of a person accused of a crime)

the lawyer is bound by all fair and honorable means, to present every defense that the law of the land permits, to the end that no person may be deprived of life or liberty, but by due process of law.”

Canon No. 15. “. . . The lawyer owes ‘entire devotion to the interest of the client, warm zeal in maintenance and defense of his rights and the exertion of his utmost learning and ability,’ to the end that nothing be taken or be withheld from him, save by the rules of law, legally applied. No fear of judicial disfavor or public unpopularity should restrain him from the full discharge of his duty. In every judicial forum the client is entitled to the benefit of any and every remedy and defense that is authorized by the law of the land, and he may expect his lawyer to assert every such remedy and defense. . . .”

It should be noted that the accused’s constitutional rights were subjected to the same type of treatment in the lower court as the Government attempts in its brief before this Honorable Court.

It is no doubt easier for the prosecution to obtain a conviction if defense counsel can be intimidated, and Constitutional rights stripped from an accused without effective protest from defense counsel. In this case the United States Government seeks to censure the defense counsel for urging error in the lower court and for urging the Constitutional rights of the accused.

Where are our Constitutional Rights, if defense counsel cannot urge them with zeal, forcibly and as clearly as possible before the United States Court of Appeals?

Where is the Constitutional Right, Sixth Amendment “to have the assistance of counsel for his de-



fense" if counsel is reprimanded and accused in such language as the United States Government used in "Brief for the United States" for urging error to the prejudice of the accused and the client's Constitutional rights?

One of the defense counsel in this case sat as a Military Court judge in Kreis Goeppingen at the start of the occupation; and there was a reluctance of Rechtsanwalts to defend the more serious offenses against the military occupation before the Military Court, for they had learned before the occupation that it was imprudent to defend certain types of cases before the German Courts. One Rechtsanwalt, Dr. Henssler, explained he always inquired first if it were prudent to defend the accused, for after the first warning, the Rechtsanwalt who persisted soon suffered consequences from the disfavor of the Nazi government or The Party. Can it be in this country, it is now imprudent to defend a client's constitutional rights or to urge error before the United States Court of Appeals? If the Government, at the taxpayer's expense, can print such a brief as appears in this case as "Brief for the United States," as a permanent record and memorial in the archives of this Court, then we submit it is imprudent to urge the Constitutional rights of an accused, or assign or urge error before this Honorable Court. If defense counsel, for seeking to protect the Constitutional rights of an accused, and urging error, and appealing to this Honorable Court by the statutory right of appeal, can be censured by the government for observing the basic and fundamental duties of counsel, then it is imprudent to accept employment, and the right to counsel is now an empty phrase.

## II.

**Computations Based Upon Investigation of Third Person's Books Not in Evidence; and Computations Not Subject to Determination as to the Various Items Nor Subject to Inspection Do Not Meet the Requirements of Fair Play.**

The prosecution has set forth a series of impressive figures on page 7 of its brief. These are the figures which were never substantiated, which were based upon work sheets not permitted to be inspected nor examined by the defense nor the jury. Neither the jury nor the defense were ever given the various items that supported the various totals going to make up the alleged income, although demanded on a dozen occasions by the defense during the course of the trial. Figures and totals are no better than the items that go to make them up, or the methods of computations in arriving that those figures and totals. The defense repeatedly demanded the "work sheets" used to arrive at these figures, but never obtained any.

Furthermore, these figures cited by the government witnesses are clearly based in some part upon items determined by the government's witnesses from their investigation of third person's books not in evidence. None of these third persons were witnesses, were sworn, or subjected to cross-examination. The identity of such informers, and the basis of the alleged items, or indeed their amounts were never disclosed; except, that some items of unknown amounts were alleged to have been obtained from unknown records of the Bureau of Public Debt.

Any accusations of the prosecution, any allegations of proof by the prosecution based upon such computations do not meet the basic requirements of fair play, nor due process of law.

## III.

**The Prosecution's Attempted Explanation of the Discrepancies Between Their First Trial Computations and Their Second Trial Computations Does Not Explain the Greater Increase in "Corrected Business Receipts" Charged in the Second Trial Computations.**

The prosecution seeks to justify the difference in testimony between the government investigators as to the amounts of alleged net income by the unsupported bare statements of Agent Krause that he "leaned over backwards" in allowing deductions (Brief, p. 8). But leaning over backwards in allowing deductions does not account for an increase of \$1200 to \$3600 in "corrected business receipts" in the Krause figures over the Tormey figures (see Appellant's Opening Brief, p. 28, for comparisons and citations into the transcript), if the same basic data and the same methods of accounting (likely to overstate income) be used by those two agents. Of course, the answers lies in determining what items went into what columns and what computations followed,—and these appear only in the "work sheets" demanded by the defense on a dozen different occasions, and refused either examination by the defense or to be put into the evidence.

The added vice appears from the consolidation of various items in the Krause computations which should to the extent of such consolidation reduce the Krause computations of "corrected business income" below the Tormey computations of the same comparable item, for a fair comparison.

## IV.

**The Prosecution Proved the Authenticity of the "Gray Book" by Comparisons With the Mysterious Check Stubs by Alleged Obliterations Not Before the Jury.**

The prosecution, page 6 of its brief, seeks to establish the proof of the execution of the disputed parts of the "gray book" by the alleged similarity to similar obliterations in the defendant's check stubs which were never in evidence. The prosecution contends in its brief that the defendant gave her receipt for the documents but did not produce them in court. The admission of the Gray Book upon the alleged proof is shown in Transcript pg. 80 and 85 et seq, and reprinted in Supplement to Appellant's Opening Brief, pages 16 to 24.

It is interesting to note that Government Agent Krause testified he used the check stubs in his computations begun after the first trial and completed just before the second trial (Transcript pg. 406) but on further cross-examination, changed his testimony and stated he was merely speculating (Transcript pg. 418-420). He must have had the check stubs in his possession to have used them in the computations.

## V.

**Naming of Deductions Which Statute Permits a Taxpayer to Take by Either Name Is Made a "Red Herring" to Prejudice the Accused.**

The prosecution makes much of the misnaming of certain deductions (Brief pg. 8) and the calling of a lawful deduction properly taken as "charitable contribution" or "gambling loss" during the years 1943 and 1942. For the year 1944 when the "standard deduction" was taken, to call a "gambling loss" a "charitable contribution" would merely work to the



disadvantage of the taxpayer, not the government.

A deduction permitted by law, is properly deductible regardless by what name it may be called by a taxpayer. Whether the taxpayer called it "good cause" or "red cross" or "gambling debt" would not defraud the government; nor would it be improper, nor would it be reprehensible.

The Indictment, First Count, alleges "deductions" as "contributions . . . \$152.50." The Prosecution's witness Krause gave the amount claimed for charitable contributions by the Witness at \$152 but contends that this is wrong. Tr. pg. 229-230. The Prosecution's Brief, pages 8 and 12, contends that the defendant's return of "contributions" for charity in Exhibit 2 for \$152 is false. We want to point out

that the prosecution's case is predicated upon the basis that both the figures in the indictment for "contributions . . . \$152.50" and the defendant's claim of the same sum in her 1942 return are erroneous. It is predicated upon the basis that the figures in the indictment second count "contributions \$255.00" and the defendant's claim of the same sum in her 1943 return are erroneous.

It is indeed a sorry state of affairs when the grand jury alleges certain figures in the indictment that the defendant sets forth in her returns are proper, and the prosecution during the trial then contends that these figures are erroneous and false, and consequently the defendant is guilty of fraud for reporting and entering the same figures charged as the proper amounts for "contributions" in the indictment.

It should be noted that the defendant's testimony

showed contributions to her Catholic Church's poor box, to various contributions solicited of many taverns and which taverns are forced to give sums to various organized charities by reason of social pressure and public opinion, and the defendant paid certain sums for masses at her Catholic Church, in addition to sums claimed.

It should be observed that for the year 1944, the defendant took the "standard deduction," which is allowed, irrespective of the amounts actually contributed to charities; and any entry in the defendant's books as to 1944 as to charities is mere surplusage and would not effect her income tax or its liability. As a gambling loss it is deductible, for the proof was that her gambling winnings including "double or nothing" at the bar with customers was substantial. As "charitable" contributions it was not deductible due to the standard deduction taken. It therefore followed that the taxpayer, not the government, would suffer prejudice by labeling a gambling loss a charitable contribution during 1944.

## VI.

### **The Exceptions Were Properly Made the Subject of Exceptions by the Defendant Before the Jury Retired.**

The instructions were settled by the Court during the trial upon a hearing in open court. The prosecution's statement that no exceptions were noted, Brief, page 24, is probably explainable by the fact that the government obtained a "daily" transcript and did not see fit to order this part of the proceedings transcribed. Defendant has ordered, transcripts of the portions of the hearing not transcribed, dealing with the contest over the instructions.

The defendant duly asked that exceptions be noted to the Court's ruling as to the giving of most of the government's proposed instructions and the refusal

to give the defendant's proposed instructions. The Court noted the exceptions.

As soon as the Court reporter has transcribed this portion of the record which has evidently been omitted, although all the record was requested by the defendant, we trust the omission in the record will be cured.

The defendant has attempted to set out the instructions in full given by the court, and those requested by the defendant and refused, in both the assignments of error and in the printed supplement to the Appellant's Opening Brief. We trust we have not misled the Court as prosecution would intimate. In Appellant's Opening Brief a few of the more flagrant errors in the instructions are outlined, and need not be repeated in this brief.

## VII.

**The Same Disclosure Was Made to Defendant's Accountant Bosserman as Was Alleged to Be Proof of Falsity During the Trial. Having Made a Full Disclosure, She Had a Right to Rely Upon the Professional Skill and Services of Her Accountant.**

The prosecution at page 21 of their brief contends that the defendant provided her accountant Bosserman with an alleged false book, Exhibit 5, claiming in the same sentence that she provided him with the "gray book," Exhibit 14, and thus she misled her accountant. The fallacy with the prosecution's argument is that the prosecution's alleged proof of a double set of entries, is predicated solely upon the entries in the Gray Book, Exhibit 14, from July 17, 1942, to August 23, 1942, were alleged entries made at the alleged dates and in the Gray Book, which, with the Black Book covering July 16, 1942, on, were

both claimed by the Government to be given to Bosserman at the time he prepared Exhibits 1 and 2, the 1942 Partnership and individual returns of the Josts. The accountant could not have been misled, for the defendant made, by the prosecution's contention, as full, fair and complete a disclosure to her accountant of the very case the prosecution made proof at the trial.

If the Gray Book, Exhibit 14, contained the disputed entries for July 17 to August 23, 1942, while the prosecution contends the book was in her possession; if she delivered the Gray Book, Exhibit 14, to Bosserman with the Black Book, Exhibit 5, and there were the discrepancies of such large sums for those dates, the accountant must have used the records to make out the returns, and a full and complete disclosure was made by the defendant of the very thing the prosecution contends is their proof and badge of fraud.

Upon the prosecution's own statement of the case, the accused made a full, fair and complete disclosure of all the facts to her accountant; it follows she did not and could not have misled him; and she has a right to rely upon his professional skill and work and make her returns upon his work.

Of course, the evidence is not that clear, and is only the statement most favorable to the prosecution's contentions. The evidence shows that Bosserman testified at the first trial he did not work from the Gray Book in making the partnership returns. The testimony shows that Bosserman, at the first phase of the agent's investigation, supplied the Agent Krause with the Gray Book. Furthermore, there are so many reasons why the Gray Book from the middle of July, 1942, on cannot be possibly the records of the defendant's business, which so clearly



appear in the record, that we have not undertaken to outline them in this Reply Brief. We fully understand the draftsman's position in the prosecution's brief, for he has fallen into the same method of thinking as defense counsel—that the disputed writings were not in the Gray Book until much later. The disputed writings not being in the Gray Book at the time the government contends Bosserman used it to make out the reports for the defendant and her husband, it is arguable that the defendant misled her accountant by providing her accountant Bosserman with but one set of figures—the Black Book, Exhibit 5, for him to prepare the husband and wife returns upon which the first count of the indictment is based. However, if the disputed writings in the Gray Book, Exhibit 14, were in the Gray Book during 1942, as the prosecution now contends, it follows that the discrepancies would immediately become apparent, and a full, fair and complete disclosure of the alleged “true income” would have been made. The accountant must then have made his return upon the very evidence offered by the prosecution as the sole basis of their case before the jury.

If the disputed items in the Gray Book, Exhibit 14, were not in it until after tax time in 1943 when 1942 returns were made out; and Government witness Bosserman held that book from tax time, 1943, until he delivered it to the Agent Krause, it is quite obviously nothing upon which the prosecution can predicate its alleged public offense against the accused. We believe that if the Court will examine the original books, Ex. 5 and Ex. 14, and actually compare the two writings themselves—as the jurors should have been instructed they were entitled to under Defendant's proposed Instruction No. 4, 28 USCA 638, the Court can see most vividly the error

of the Court in refusing the instruction, the miscarriage of justice thereby, and the damage of the defendant's case, and contention as to the disputed writing.

If the writing were in the Gray Book, Exhibit 14, at the end of 1942 or early 1943, then the defendant made a full, fair and complete disclosure to her accountant by delivering to him that book as the prosecution contends she did, and the alleged case of fraud falls of its own weight and from the Government's proof.

### VIII.

#### **The Failure to Provide the Bill of Particulars Resulted in Serious Prejudice and Surprise.**

The Prosecution, in its brief, pages 9-11, contends there was no prejudice and the accounts were offered the defendant; and contends because it was the second trial that there were the same witnesses with minor exceptions.

The first trial was had upon the Agent Tormey computations and we trust we have demonstrated in the opening brief the material difference between those amounts and the amounts sprung at the second trial upon the Agent Krause computations. A reading of the record will show the material differences in testimony from the first trial where repeated references appear to the first account of the prosecution and its differences from the second. See Appellant's Opening Brief, pages 4 to 8, 28 for tabulations of some of these differences. See pages 5 to 15, Supplement in Appellant's Opening Brief, for proceedings for Bill of Particulars and affidavits in support.

No offer of any detailed records or schedules were ever made to the defense as contended at page 11 of prosecution's brief, and citation of Record pages

484-5, Transcript 414-5. That was merely where, on cross-examination Agent Krause was asked for the amounts allocated in the breakdown spent for entertainment in connection with the business of the defendant, the witness answered that in his schedule of all disbursements made, he broke them down into deductible and non-deductible items, into capital and loan items but not classified as entertainment items. No offer was made to defense counsel to inspect them, and repeated demands were made to inspect them and to put them into the evidence. Indeed the first demand for the work sheets was made during the noon recess and demand in Open Court for the order for permission to examine the work sheets appear on Transcript, pg. 447-452. Again it was made, Tr. 478, the following morning upon the commencement of the next day of trial. See Opening Brief, pages 33-6, and Suppl., pg. 43-46, 50-52, and 55. It is interesting to note that at no time did the prosecution counsel contend that defense had refused to examine the Krause "work sheets" nor put them into evidence as now claimed in prosecution's brief, pages 9 to 11. They knew that defense counsel had at the first trial examined the Tormey worksheets, and their case would not stand similar inspection if the defense were granted the same opportunities to show to the jury how the Krause worksheets would not and could not support the figures upon which the prosecution built the second trial. We note with interest the prosecution's contention, on page 11 of their brief: "The Government refused to accede to the latter request, as the thousands of items involved would have but further encumbered the record and they were nothing but recapitulations of matters already in the record." Defendant was *surprised* to learn that the government's figures

involved matters determined from outside investigation and not confined to the records of the case. Tr. pg. 646-7. Indeed, this was the only way that such alleged income could have been arrived at. See affidavits for Bill of Particulars, Suppl. pages 7 to 15; but the defense was misled by the testimony of Government counsel on the bill of particulars, see Tr. of Sept. 2, 1947, on Bill of Particulars proceeding.

It should be observed that when an income tax indictment allegations can be proved by testimony of a Government agent that the defendant made such and such income, and the Government can refuse the right to the defense to inquire into the items that made up the computation and to see what items went into income and which are allowed as deductions, and the computations thereon, and the Court will prevent such inquiry and testimony, a mere charge of guilt carries through to a conviction and the essence of due process of law does not exist in such trials. This is trial by denunciation.

“Denunciation” is a term of the “civil law” used on the continent of Europe meaning the charge laid before the public prosecutor upon which the criminal proceedings are usually started.

*Bouvier's Law Dictionary* (Banks Ed.) P. 292.

*Black's Law Dictionary*, (2nd Ed), Pg. 354.

A trial by denunciation means that the mere lodging of the charge results in prosecution and conviction; the denunciation is in reality the determination of guilt and the rest follows as a formality. For example, a charge is lodged by certain Government agents; and this denunciation is lodged in the dossier of the accused and the rest is a mere formality from the review by the various higher offices through the prosecutor's office, and the denunciation suffices to con-



vict the accused and criminality and disability of conviction and sentence follow.

We have gone to great lengths in our Opening Brief to point out how and why this is what obtains in the instant case. We would be remiss in our duty as counsel if we did less. Now it appears we stand censured by our United States Government in a printed memorial in the archives of this Honorable Court. Is it now imprudent to urge error or plead an accused's Constitutional rights before this Honorable Court? Is this now reprehensible? Will diligence and good judgment require counsel to forbear to plead error in the trial of an accused or to urge the constitutional rights before this court?

## IX.

### **The Laws of California as to Community Property Are Necessary for the Determination of the Income of the Defendant.**

There is no issue that the domicile of the defendant and her husband were in California from their marriage in early 1942 to dissolution of the marriage in the middle of 1944. The law of the domicile of the parties, California, and the situs of all their property, real and personal, also California, governs their rights. All property acquired after marriage, with certain exceptions, is Community Property.

#### *Civil Code 161a, 164*

It is a general rule that money borrowed on personal security by a husband or wife is community property.

*Mosesian v. Parker*, 44 Cal. App. 2d 544, 112 P.

(2d) 705;

*Moulton v. Moulton*, 182 Cal. 185, 187 P. 421.

Earnings of a wife from her personal services while living with her husband are community property.

*Martin v. Southern Pac. Co.*, 130 Cal. 285, 62 P. 515;

*Henry v. Hibernia Sav. & Loan Soc.*, 5 Cal. App. 2d 141, 42 P. (2d) 395.

And the proceeds of earnings, community property, are also community property.

*Crossan v. Crossan*, 35 Cal. App. 2d 39, 94 P. (2d) 609.

Where community property is commingled, and each part is not clearly ascertainable and traceable, the presumption is in favor of community property.

*Estate of Fellows*, 106, Cal. App. 681, 289 P. 887;

*Falk v. Falk*, 48 Cal. App. 2d 762, 120 P. (2d) 715.

Community funds, as for example earnings that are community, used in improving the separate property of a spouse retain their character as community property.

*Provost v. Provost*, 102 Cal. App. 775, 283 P. 842;

*Chandler v. Chandler*, 112 Cal. App. 601, 297 P. 636.

Where portion of the accumulations or income are services or skill that are community property, those portions are community although the business was separate property of a spouse.

*Lawrence Oliver v. Comm'r.*, 4 Tax Court 684;  
*Periera v. Periera*, 156 Cal. 1, 103 P. 488;

*In re McCarthy's Estate*, 127 Cal. App. 80, 15 P. (2d) 223.

The testimony of both the Government witness Jost and the defendant were that the husband dur-

ing the entire time he lived with the accused, took his earnings and used them in the business and drew what he needed from the business. Half the business, claimed by the prosecution to be of little value in January, 1942, was separate property of the accused. The other half was acquired by money borrowed upon personal credit, and from saved earnings of the community. The principal income was the services and skill of the husband and wife in running the tavern. For the first time in California law, it appears to be urged by the prosecution that because the accused used her first married name of Larson (Pros. Brief 25), that her earnings while living with her husband were not community property.

The fact remains that under California law, the wife's interest in community property is a vested one-half interest, which she must report as income. The other half is income of the husband which he must report. He has the management and control of the community property. Yet the prosecution contends that the law of husband and wife in the domicile of the parties and the situs of the property, California, is no part of the case and the wife is chargeable with all the income of the community, and even the husband's earnings during 1942 prior to their marriage, for the purpose of computing income tax upon a charge of feloniously attempting to evade the income tax.

The prosecution's case is predicated upon the assumption that gift of community property ("relinquishment") makes receipt of a gift taxable income. The prosecution's case is predicated upon the assumption that a wife who follows the usual practice in divorce cases of relying upon the presumption that property in her possession is presumed to be

separate property, and alleges that at the time she filed the action for divorce that no community property remains (it having been spent or transferred into separate property) must be chargeable with all the income of the husband, and she is guilty of a felony for failure to report his, her divorced husband's income.

### CONCLUSIONS

The prosecution has failed to comment upon the failure of the Government to call Agent Tormey; that the defendant did so and was not permitted to examine him as an adverse witness. See Appellant's Opening Brief, pages 14 to 18. We take it that this point is conceded.

We trust in our limited space of a Reply Brief, that we have demonstrated a few of the fallacies and erroneous contentions that appeared in the prosecution's brief.

We trust the record supports amply the accused's request for a directed verdict on each count, and her specifications of error as we have attempted to point out in our limited space.

HYMAN & HYMAN,  
HOWARD B. CRITTENDEN, JR.,

Central Tower Building,  
San Francisco, California,

*Attorneys for Appellant.*



No.11912

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United States  
Circuit Court of Appeals  
For the Ninth Circuit.

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THE DAVENPORT FOUNDATION,  
Petitioner,  
vs.  
COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

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Transcript of the Record

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Upon Petition to Review a Decision of the Tax Court  
of the United States

FILED

JUN 24 1948

PAUL P. O'BRIEN,

CLERK









No. 11912

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United States  
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# INDEX

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

	PAGE
Amended Petition.....	23
Answer .....	22
Answer to Amended Petition.....	26
Appearances .....	1
Certificate of Clerk.....	152
Decision .....	43
Docket Entries.....	2
Memorandum Findings of Fact and Opinion...	28
Findings of Fact.....	28
Opinion .....	37
Notice of Filing Petition to Review Decision of The Tax Court of the United States.....	51
Petition .....	4
Exhibit A—Notice of Deficiency.....	7
Petition to Review Decision of The Tax Court of the United States.....	44
Praeipue for Transcript.....	151
Statement of Evidence Agreed to and Exhibits Attached .....	52

	INDEX	PAGE
Witnesses for Petitioner:		
Allard, Joseph A., Jr.		
—direct .....		52
—cross .....		59
Crippen, Mrs. Elizabeth		
—direct .....		73
—cross .....		73
Davenport, Homer H.		
—direct .....		69
—cross .....		70
Davenport, John R.		
—direct .....		70
—cross .....		71
Flora, Fred A.		
—direct .....		71
—cross .....		72
Steinour, J. E.		
—direct .....		59
—cross .....		64
—redirect .....		65
—recross .....		66
Weller, Mrs. Lucile		
—direct .....		66
—cross .....		68



## INDEX

## PAGE

## Joint Exhibits:

1- A—Declaration of Trust.....	84
By-Laws of the Davenport Foundation .....	98
4- D—Transfer and Acceptance of Additional Property Under Trust .....	108
5- E—Grant Deed Corporation.....	110
6- F—Resolution .....	112
7- G—Grant Deed Corporation.....	113
8- H—Articles of Incorporation for Non-Profit Corporation.....	114
9- I—By-Laws of the Davenport Foundation .....	124
10- J—Resolution .....	135
11- K—Grant Deed Corporation.....	137
12- L—Corporation Grant Deed.....	138
13- M—Grant Deed.....	139
14- N—Annuity Agreement.....	139
15- O—Grant Deed.....	144
16- P—Annuity Agreement.....	144
17- Q—Taxable Net Income.....	149

Statement of Points on Which Appellant In- tends to Rely and Designation of Parts of the Record Necessary for Consideration.....	154
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## APPEARANCES

For Petitioner:

MELVIN D. WILSON, ESQ.,  
JOSEPH D. PEELER, ESQ.,  
J. REX DIBBLE, ESQ.

For Respondent:

E. A. TONJES, ESQ.

Docket No. 10427

THE DAVENPORT FOUNDATION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## DOCKET ENTRIES

1946

- Apr. 1—Petition received and filed. Taxpayer notified. Fee paid.
- Apr. 1—Copy of petition served on General Counsel.
- May 8—Answer filed by General Counsel.
- May 8—Request for hearing at Los Angeles, California, filed by General Counsel.
- May 10—Notice issued placing proceedings on Los Angeles, California, calendar. Service of answer and request made.
- Dec. 6—Hearing set 2/10/47 at Los Angeles, California.

1947

- Feb. 14—Appearance of J. Rex Dibble as counsel filed at hearing in Los Angeles.
- Feb. 14—Hearing had before Judge Leech on merits. Motion of petitioner to amend petition—granted, stipulation of facts and ap-



1947

pearance of J. Rex Dibble filed at hearing. Petitioner's brief 4/28/47. Respondent's brief 6/2/47. Petitioner's reply brief 7/2/47.

Mar. 1—Hearing had before Judge Leech. Stipulation filed at hearing and answer to amended petition. Copies served.

Mar. 5—Transcript of hearing 2/14/47 filed.

Apr. 28—Brief filed by taxpayer. Copy served.

May 16—Reply brief filed by General Counsel. Copy served.

June 30—Reply brief filed by taxpayer. 7/1/47 Copy served.

Dec. 24—Memorandum findings of fact and opinion rendered. Judge Leech. Decision will be entered for the respondent. 12/26/47 Copy served.

Dec. 29—Decision entered. Judge Leech, Div. 6.

1948.

Mar. 24—Petition for review by U. S. Circuit Court of Appeals, 9th Circuit, with assignments of error filed by taxpayer.

Mar. 24—Proof of service filed.

Apr. 19—Statement of evidence filed by taxpayer with service acknowledged thereon.

Apr. 19—Praecipe for record filed by taxpayer with service acknowledged thereon. [1\*]

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\*Page numbering appearing at top of page of original certified Transcript of Record.

The Tax Court of the United States

Docket No. 10427

THE DAVENPORT FOUNDATION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency, LA:IT:90D:PAK, dated March 1, 1946, and as a basis of its proceeding alleges as follows:

1. The petitioner is a corporation with its principal office at 674 Elliott Drive, Pasadena, California. The returns for the period here involved were filed with the Collector for the Sixth District of California.

2. The Notice of Deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner on March 1, 1946.

3. Taxes in controversy are Federal corporate income tax and declared value excess profits tax as follows:

Income Tax	
1940.....	\$ 468.02
1941.....	1,415.13
1942.....	2,292.63
1943.....	2,272.00
1944.....	2,804.44
	<hr/>
	\$9,252.22

	Declared Value	Excess-Profits Tax
1941.....		\$ 409.20
1942.....		300.11
1943.....		86.30
		<hr/>
		\$ 795.61

4. The determination of tax set forth in the said Notice of Deficiency is based upon the following errors:

(a) The respondent erred in failing to hold that petitioner is exempt from Federal corporate income and declared value excess profits tax under the provisions of Sections 101(6), 600, 1200 and 1201 (a)(1) of the Internal Revenue Code.

5. The facts upon which petitioner relies as a basis of this proceeding are as follows:

(a) The petitioner was organized on or about June 5, 1940, as a non-profit corporation under the provisions of Title XII, Article 1 of the General Non-Profit Corporation Laws of California, exclusively for religious, charitable, scientific, literary and educational purposes; no part of the net earnings were to inure to the benefit of any private shareholder or individual and no substantial part of the activities of which was to carry on propaganda or otherwise attempt to influence legislation.

(b) In 1940 and 1941 Levi M. Davenport and his wife, Barbara N. Davenport, transferred or caused to be transferred to petitioner properties of a total value of \$270,384.00, in part consideration for which petitioner agreed to let the Davenports use one of the properties as their living place and agreed to pay over to the Davenports or to their

daughter or granddaughter certain annuities, all of which rights retained by the Davenports and assumed by petitioner had a value not in excess of \$90,315.38, with the result [3] that petitioner received a net gift of at least \$180,068.62.

(c) Petitioner throughout its existence was and is a corporation organized and operating exclusively for religious, charitable, scientific, literary or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual and no substantial part of the activities of which is carrying on propaganda or otherwise attempting to influence legislation.

(c) None of petitioner's net income was subject to income tax within the provisions of Sections 101(6), 600, 1200 and 1201(a)(1) of the Internal Revenue Code for any of the years 1940 to 1944, inclusive.

Wherefore, petitioner prays that the Court hear this proceeding and determine that petitioner is exempt from Federal corporate income and declared value excess profits tax for the years 1940 to 1944, inclusive.

/s/ MELVIN D. WILSON,

/s/ JOSEPH D. PEELER,

Counsel for Petitioner. [4]



State of California,  
County of Los Angeles—ss.

Fred A. Flora and J. E. Steinour, being duly sworn, depose and say that they are the Secretary and Treasurer of The Davenport Foundation and are duly authorized to verify the foregoing petition; that they have read the foregoing petition and are familiar with the statements contained therein and that the statements contained therein are true except those stated to me upon information and belief and that those they believe to be true.

/s/ FRED A. FLORA,

/s/ J. E. STEINOUR.

Subscribed and Sworn to before me this 29th day of March, 1946.

[Seal] /s/ NORMA LUND,

Notary Public in and for Said  
County and State.

My Commission Expires August 8, 1949. [5]

#### EXHIBIT A

Treasury Department, Internal Revenue Service,  
417 South Hill Street, Los Angeles 13, California. Office of Internal Revenue Agent in Charge, Los Angeles Division. LA:IT:90D:PAK.

Mar. 1, 1946.

The Davenport Foundation  
674 Elliott Drive  
Pasadena, California

Gentlemen:

You are advised that the determination of your income tax liability for the taxable years ended

December 31, 1940, 1941, 1942, 1943 and 1944, discloses a deficiency of \$9,252.22, and that the determination of your declared value excess-profits tax liability for the taxable years ended December 31, 1941, 1942 and 1943, discloses a deficiency of \$795.61, as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Los Angeles, California, for the attention of LA:Conf. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form,

or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,

Commissioner.

By GEORGE D. MARTIN,

Internal Revenue Agent in

Charge.

Enclosures :

Statement

Form of waiver. [7]

## STATEMENT

LA:IT:90D:PAK

The Davenport Foundation, 674 Elliott Drive  
Pasadena, California

Tax Liability for the Taxable Years Ended  
December 31, 1940 to 1944, inclusive

Income Tax			
Year	Liability	Assessed	Deficiency
1940 .....	\$ 468.02	\$0.00	\$ 468.02
1941 .....	1,415.13	0.00	1,415.13
1942 .....	2,292.63	0.00	2,292.63
1943 .....	2,272.00	0.00	2,272.00
1944 .....	2,804.44	0.00	2,804.44
	<hr/>	<hr/>	<hr/>
Totals .....	\$9,252.22	\$0.00	\$9,252.22

Declared Value Excess-Profits Tax			
1941 .....	\$ 409.20	\$0.00	\$ 409.20
1942 .....	300.11	0.00	300.11
1943 .....	86.30	0.00	86.30
	<hr/>	<hr/>	<hr/>
Totals .....	\$ 795.61	\$0.00	\$ 795.61

In making this determination of your tax liability, careful consideration has been given to the report of examination dated October 30, 1945.

The contention in your returns that your corporation is exempt from taxation in accordance with the provisions of section 101(6) of the Internal Revenue Code is denied.

The deduction claimed for depreciation in the amount of \$169.65 for the taxable year ended December 31, 1940, and \$339.30 for each of the taxable years [8] ended December 31, 1941, to 1944, inclusive, on property designated as 674 Elliott Drive, Pasadena, California, is disallowed. This property is occupied by Mr. Davenport as his personal residence and no rental is paid by him for the use of this property. It has been determined that the deductions claimed for depreciation on this property are not allowable under Section 23(1) of the Internal Revenue Code.



In your returns you computed depreciation on certain parcels of improved real estate on the basis of the appraised values thereof at the date such properties were acquired by you. It has been determined that the correct basis for computing depreciation on these properties as provided in section 114(a) of the Internal Revenue Code is as follows:

Designation of Property	Basis Claimed In Returns		Basis Determined	
	Land	Improvements	Land	Improvements
8648 Atlantic, Southgate, Calif.....	\$ 1,020.00	\$ 2,300.00	\$ 1,020.00	\$ 1,800.00
8670 Atlantic, Southgate, Calif.....	6,630.00	14,975.00	6,630.00	16,000.00
8680 Atlantic, Southgate, Calif.....	8,160.00	17,575.00	8,160.00	14,401.77
4623 E. Gage, Bell, California.....	5,000.00	3,000.00	5,000.00	1,050.00
Bloom Street, Los Angeles, Calif.....	1,300.00	2,700.00	1,300.00	2,000.00
106 So. Broadway, Los Angeles, Calif.....	12,000.00	8,000.00	12,000.00	3,600.00
152 So. Eastman, Los Angeles, Calif.....	1,500.00	5,100.00	1,500.00	5,900.00
2326 E. Eighth St., Los Angeles, Calif.....	7,000.00	9,000.00	7,000.00	7,931.64
228 E. First St., Los Angeles, Calif.....	22,000.00	18,000.00	22,000.00	440.00
2470 E. Fourteenth St., Los Angeles, Calif. }	Leased	10,850.00	Leased	8,748.13
2530 E. Fourteenth St., Los Angeles, Calif. }				
Mason Street, Southgate, California.....	0.00	1,491.27	0.00	740.00
Totals.....	\$64,610.00	\$92,991.27	\$64,610.00	\$62,611.54

*The Davenport Foundation vs.*

These properties were acquired by you on or about July 1, 1940, and it has been determined that each property has a remaining useful life of 25 years from that date. The property designated as 405-11 Wall Street, Los Angeles, California, has been determined to have a useful life of 25 years from date of acquisition, July 1, 1942, instead of 40 years as shown by your returns.

The amount of excessive deductions claimed for depreciation under section 23(1) of the Internal Revenue Code is determined by the following:

	1940 (Six Mos.)	1941	1942	1943	1944
8648 Atlantic, Southgate, Calif.....	\$ 36.00	\$640.00	\$640.00	\$640.00	\$640.00
8670 Atlantic, Southgate, Calif.....	320.00	576.07	576.07	576.07	288.03
8680 Atlantic, Southgate, Calif.....	288.03	42.00	42.00	42.00	42.00
4623 E. Gage, Bell, California.....	21.00	80.00	---	---	---
Bloom Street, Los Angeles, Calif.....	40.00	144.00	144.00	144.00	144.00
106 So. Broadway, Los Angeles, Calif.....	72.00	236.00	236.00	196.67	---
152 So. Eastman, Los Angeles, Calif.....	118.00	17.60	17.60	17.60	17.60
228 E. First St., Los Angeles, Calif.....	8.80	317.27	317.27	317.27	317.27
2326 E. Eighth St., Los Angeles, Calif.....	158.63	349.93	349.93	349.93	349.93
2470 E. Fourteenth St., Los Angeles, Calif. }	174.96	29.60	29.60	29.60	7.40
2530 E. Fourteenth St., Los Angeles, Calif. }	14.80	240.00	240.00	480.00	480.00
Mason Street, Southgate, California.....	---	---	---	---	---
405-11 Wall Street, Los Angeles, Calif.....	---	---	---	---	---
Totals (depreciation allowable).....	\$1,252.22	\$2,432.47	\$2,592.47	\$2,793.14	\$2,286.23
Depreciation claimed on these properties in your returns .....	1,509.84	2,865.82	2,912.44	3,016.73	2,548.47
Excessive amount claimed.....	\$ 257.62	\$ 433.35	\$ 319.97	\$ 223.59	\$ 262.24

The excessive deductions claimed are disallowed.

Adjustments to Net Income  
Taxable Year Ended December 31, 1940

Net income as disclosed by return.....		\$2,745.70
Unallowable deductions:		
(a) Unallowable depreciation.....	169.65	
(b) Excessive depreciation .....	257.62	427.27
		<hr/>
Total .....		\$3,172.97
Additional deduction:		
(c) Deduction for contributions increased.....		21.36
		<hr/>
Net income adjusted.....		\$3,151.61

Explanation of Adjustments

(a) and (b) These adjustments have been previously explained.

(c) Due to the increase of net income shown above the deduction for contributions has been increased by 5 per centum of such increase, or \$21.36, in accordance with section 23(q) of the Internal Revenue Code.

Computation of Income Tax  
Taxable Year Ended December 31, 1940

Net income adjusted .....	\$3,151.61
Normal—tax net income.....	3,151.61
Income tax:	
Normal tax—13½% of \$3,151.61.....	425.47
Defense tax—10 % of 425.47.....	42.55
	<hr/>
Correct income tax liability.....	468.02
Income tax assessed	
Original, account No. 9200902.....	None
	<hr/>
Deficiency of income tax.....	468.02

Adjustments to Net Income  
Taxable Year Ended December 31, 1941

Net income as disclosed by return.....		\$5,244.12
Unallowable deductions and additional income:		
(a) Unallowable depreciation .....	339.30	
(b) Excessive depreciation .....	433.35	
(c) Net long-term capital gain in- creased .....	641.43	1,414.08
		<hr/>
Total .....		\$6,658.20

## Additional deduction:

(d) Deduction for contributions increased.....	70.70
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Net income adjusted.....	\$6,587.50
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## Explanation of Adjustments

(a) and (b) These adjustments have been previously explained.

(c) In lieu of the long-term capital gain of \$39.84 reported in your return from the sale of a parcel of real estate designated as 8648 Atlantic Boulevard, Southgate, California, it has been determined that you realized a long-term capital gain of \$681.27 or an increase of \$641.43.

(d) Due to the increase in net income as shown herein in the amount of \$1,414.08 the deduction for contributions has been increased by 5 per centum thereof, or \$70.70, in accordance with section 23(q) of the Internal Revenue Code.

## Computation of Declared Value Excess-Profits Tax

## Taxable Year Ended December 31, 1941

Net income adjusted .....	\$6,587.50
Less: 10% of \$27,900.00 value of capital stock as declared in capital stock tax return for the year ended June 30, 1941.....	2,790.00

Net income subject to declared value excess-profits tax .....	3,797.50
Amount taxable @ 6.6% (5% of \$27,900.00).....	1,395.00

Amount taxable @ 13.2% .....	\$2,402.50
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## Declared value excess-profits tax:

6.60% of \$1,395.00.....	\$92.07
13.2% of 2,402.50.....	317.13

Correct declared value excess-profits tax liability....	\$ 409.20
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## Declared value excess-profits tax assessed:

Original, account No. 9200903.....	None
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Deficiency of declared value excess-profits tax.....	409.20
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Computation of Income Tax  
Taxable Year Ended December 31, 1941

Net income adjusted.....	6,587.50
Normal-tax net income.....	6,587.50
Surtax net income .....	6,587.50
Income tax:	
Normal tax: 15% of \$5,000.00.....	750.00
17% of 1,587.50.....	269.88
	<hr/>
Surtax: 6% of 6,587.50.....	395.25
	<hr/>
Correct income tax liability.....	1,415.13
Income tax assessed:	
Original, account No. 9200903.....	None
	<hr/>
Deficiency of income tax .....	1,415.13

Adjustments to Net Income  
Taxable Year Ended December 31, 1942

Net income as disclosed by return.....	7,080.25
Unallowable deductions and additional income:	
(a) Unallowable depreciation .....	339.30
(b) Excessive depreciation .....	319.97
(c) Long-term capital gain.....	1,241.56
	<hr/>
Total .....	8,981.08
Additional deduction:	
(d) Deduction for contributions increased.....	95.04
	<hr/>
Net income adjusted.....	\$8,886.04

Explanation of Adjustments

(a) and (b) These adjustments have been previously explained.

(c) In lieu of the long-term capital loss of \$911.96 reported in your return from the sale of real estate designated as Bloom Street property it has been determined that you realized a long-term capital gain of \$329.60 on account of this transaction, or an increase of \$1,241.56.

(d) Due to the increase in net income of \$1,900.83 shown herein the deduction claimed for contributions has been increased by 5 per centum thereof, or \$95.04, in accordance with section 23(q) of the Internal Revenue Code.

*The Davenport Foundation vs.*

Computation of Declared Value Excess-Profits Tax  
Taxable Year Ended December 31, 1942

Net income adjusted.....	\$8,886.04
Less: 10% of \$52,900.00 value of capital stock as declared in capital stock tax return for the year ended June 30, 1942.....	5,290.00
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Net income subject to declared value excess-profits tax .....	3,596.04
Amount taxable @ 6.6% (5% of \$52,900.00).....	2,645.00
<hr/>	
Amount taxable @ 13.2%.....	951.04
Declared value excess-profits tax:	
6.6% of \$2,645.00.....	\$174.57
13.2% of 951.04.....	125.54
<hr/>	
Correct declared value excess-profits tax liability	300.11
Declared value excess-profits tax assessed:	
Original, account No. 9200904.....	None
<hr/>	
Deficiency of declared value excess-profits tax.....	\$ 300.11

Computation of Income Tax  
Taxable Year Ended December 31, 1942

Net income adjusted.....	\$8,886.04
Normal-tax net income.....	8,886.04
Surtax net income.....	8,886.04

Computation under General Rule  
(Sections 14 and 15 I. R. C.)

Normal tax:	
15% of \$5,000.00.....	\$750.00
17% of 3,886.04.....	660.63
<hr/>	
Surtax:	
10% of \$8,886.04.....	888.60
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Total income tax under general rule.....	\$2,299.23

Computation of Alternative Tax  
(Section 117 (c) (1) I. R. C.)

	Normal Tax Net Income	Surtax Net Income
Income as above.....	\$8,886.04	\$8,886.04
Minus: Excess of net long-term capital gain over net short-term cap- ital loss.....	329.60	329.60
Ordinary income.....	8,556.44	8,556.44
Normal tax:		
15% of \$5,000.00.....	750.00	
17% of 3,556.44.....	604.59	1,354.59
Surtax:		
10% of \$8,556.44.....		855.64
Partial tax.....		2,210.23
Plus: 25% of \$329.60.....		82.40
Total alternative tax.....		\$2,292.63
Correct income tax liability (Alternative tax).....		\$2,292.63
Income tax assessed:		
Original, account No. 9200904.....		None
Deficiency of income tax.....		\$2,292.63

Adjustments to Net Income  
Taxable Year Ended December 31, 1943

Net income as disclosed by return.....	\$7,577.82
Unallowable deductions and additional income:	
(a) Unallowable depreciation .....	\$339.30
(b) Excessive depreciation .....	223.59
(c) Long-term capital gain increased .....	826.37
Total .....	1,389.26
Net income adjusted.....	\$8,967.08
Additional deduction:	
(d) Deduction for contributions increased.....	69.46
Net income adjusted.....	\$8,897.62

## Explanation of Adjustments

(a) and (b) These adjustments have been previously explained.

(c) In lieu of the long-term capital gain of \$691.28 reported in your return from the sale of real estate, designated as 152 Eastman Street property, it has been determined that you realized a long-term capital gain from this transaction in the amount of \$1,517.65, or an increase of \$826.37.

(d) Due to the increase of \$1,389.26 in net income shown herein the deduction claimed for contributions is increased by 5 per centum thereof in accordance with section 23(q) of the Internal Revenue Code.

## Computation of Delared Value Excess-Profits Tax

Taxable Year Ended December 31, 1943

Net income adjusted.....	\$8,897.62
Less: 10% of \$75,900.00 value of capital stock as declared in capital stock tax return for the year ended June 30, 1943.....	7,590.00
Net income subject to declared value excess-profits tax .....	\$1,307.62
Declared value excess-profits tax:	
6.6% of \$1,307.62.....	\$ 86.30
Correct declared value excess-profits tax liability....	86.30
Declared value excess-profits tax assessed:	
Original, account No. 9200605.....	None
Deficiency of declared value excess-profits tax.....	\$ 86.30

## Computation of Income Tax

Taxable Year Ended December 31, 1943

Net income adjusted.....	\$8,897.62
Normal-tax net income.....	8,897.62
Surtax net income.....	8,897.62

## Computation under General Rule

(Sections 14 and 15 I. R. C.)

Normal tax:	
15% of \$5,000.00.....	\$750.00
17% of 3,897.62.....	662.60
Surtax:	
10% of 8,897.62.....	889.76



Computation of Alternative Tax  
Section 117 (c) (1) I. R. C.

	Normal Tax Net Income	Surtax Net Income
Income as above.....	\$8,897.62	\$8,897.62
Less: Excess of net long-term capital gain over net short-term capital loss .....	1,517.65	1,517.65
Ordinary income .....	\$7,379.97	\$7,379.97
Normal tax:		
15% of \$5,000.00.....	\$750.00	
17% of 2,379.97.....	404.59	\$1,154.59
Surtax:		
10% of 7,379.97.....		738.00
Partial tax.....		1,892.59
Plus: 25% of \$1,517.65.....		379.41
Total alternative tax.....		\$2,272.00
Correct income tax liability (alternative tax).....		2,272.00
Income tax assessed:		
Original, account No. 9200905.....		None
Deficiency of income tax.....		\$2,272.00

Adjustments to Net Income  
Taxable Year Ended December 31, 1944

Net income as disclosed by return.....	\$9,039.00
Unallowable deductions and additional income:	
(a) Unallowable depreciation .....	\$339.30
(b) Excessive depreciation .....	262.24
(c) Long-term capital gain in- creased .....	\$1,489.13
Total .....	\$2,090.67
Net income adjusted .....	\$11,129.67
Additional deduction:	
(d) Deduction for contributions increased.....	168.05
Net income adjusted .....	\$10,961.62

## Explanation of Adjustments

(a) and (b) These adjustments have been previously explained.

(c) In your return there was reported a long-term capital gain of \$1,270.36 from the sale of properties, designated as 8680 Atlantic and Mason Street, during this taxable year. It has been determined that you realized a long-term capital gain of \$1,785.34 upon the sale of the property designated as 8680 Atlantic, and a long-term capital gain of \$974.15 upon the sale of the Mason Street property, or a total of \$2,759.49. The increase in long-term capital gain of \$1,489.13 is added to your income.

(d) In computing the deduction for contributions claimed in your return you did not include in income the long-term capital gain shown by your return. It has been determined that the correct deduction for contributions under section 23(q) of the Internal Revenue Code is \$576.93 instead of the amount, \$408.88, claimed in your return, or an increase of \$168.05, as shown in the following:

Net income as disclosed by return.....	\$9,039.00
Add: Contributions claimed in re- turn .....	408.88
Increase in income as above (items (a) (b) and (c))..	2,090.67
	<hr/>
Net income adjusted before deduction for con- tributions .....	\$11,538.55
Correct deduction for contributions (5% of \$11,538.55) .....	576.93
Deduction claimed for contributions.....	408.88
	<hr/>
Additional deduction allowed.....	\$ 168.05

## Computation of Income Tax

Taxable Year Ended December 31, 1944

Net income adjusted.....	\$10,961.62
Normal-tax net income.....	10,961.62
Surtax net income.....	10,961.62

Computation under General Rule  
(Sections 14 and 15 I. R. C.)

Normal tax:

15% of \$5,000.00.....	\$ 750.00	
17% of 5,961.62.....	1,013.48	1,763.48

Surtax:

10% of 10,961.62.....		1,096.16
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Total income tax under general rule.....		\$2,859.64
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Computation of Alternative Tax  
(Section 117 (c) (1) I. R. C.)

	Normal Tax Net Income	Surtax Net Income
Income as above.....	\$10,961.62	\$10,961.62
Less: Excess of net long-term capital gain over short-term capital loss	2,759.49	2,759.49

Ordinary income .....	\$ 8,202.13	\$ 8,202.13
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Normal tax:

15% of \$5,000.00.....	750.00	
17% of 3,202.13.....	544.36	1,294.36

Surtax:

10% of 8,202.13.....		820.21
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Partial tax .....		2,114.57
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Plus: 25% of \$2,759.49.....		689.87
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Total alternative tax.....		\$2,804.44
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Correct income tax liability (alternative tax).....		2,804.44
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Income tax assessed:

Original, account No. 9200906.....		None
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Deficiency of income tax.....		\$2,804.44
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[Endorsed]: Filed April 1, 1946. [20]

[Title of Tax Court and Cause.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

1 and 2. Admits the allegations contained in paragraphs 1 and 2 of the petition.

3. Admits that the taxes in controversy are Federal corporate income tax and declared value excess profits tax; denies the remainder of the allegations contained in paragraph 3 of the petition.

4. Denies the allegations of error contained in subparagraph (a) of paragraph 4 of the petition.

5. Denies the allegations of fact contained in subparagraphs (a) to (c), inclusive, of paragraph 5 of the petition. [21]

6. Denies each and every allegation contained in the petition not hereinbefore specifically admitted or denied.

Wherefore, it is prayed that the determination of the Commissioner be approved.

/s/ J. P. WENCHEL, ECC

Chief Counsel, Bureau of  
Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel.

E. C. CROUTER,  
B. M. COON,

Special Attorneys,

Bureau of Internal Revenue.

BMC/ftc 5/2/46

[Endorsed]: Received and filed May 8, 1946. [22]



[Title of Tax Court and Cause.]

### AMENDED PETITION

The above named petitioner hereby files its amended petition pursuant to permission granted by the Court at the hearing in Los Angeles, California, on February 14, 1947, for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency, LA:IT: 90D:PAK, dated March 1, 1946, and as a basis of its proceeding alleges as follows:

1. The petitioner is a corporation, with its principal office at 674 Elliott Drive, Pasadena, California. The returns for the period here involved were filed with the Collector for the Sixth District of California.

2. That Notice of Deficiency, a copy of which was attached to the original petition and marked Exhibit A, was mailed to the petitioner on March 1, 1946.

3. The taxes in controversy are Federal corporate income and declared value excess profits taxes as follows: [23]

Income Tax	
1940.....	\$ 468.02
1941.....	1,415.13
1942.....	2,292.63
1943.....	2,272.00
1944.....	2,804.44
	<hr/>
	\$9,252.22

Declared Value Excess-Profits Tax	
1941.....	\$ 409.20
1942.....	300.11
1943.....	86.30
	<hr/>
	\$ 795.61

4. The determination of tax set forth in the said Notice of Deficiency is based upon the following errors:

(a) The respondent erred in failing to hold that petitioner is exempt from Federal corporate income and declared value excess profits tax under the provisions of Sections 101(6), 600, 1200 and 1201(a) (1) of the Internal Revenue Code.

(b) In the alternative, respondent erred in failing to hold that petitioner is exempt from Federal corporate income and declared value excess profits tax under the provisions of Section 101(14), 600, 1200 and 1201(a) (1) of the Internal Revenue Code.

5. The facts upon which petitioner relies as a basis of this proceeding are as follows:

(a) The petitioner was organized on or about June 5, 1940, as a non-profit corporation under the provisions of Title XII, Article 1 of the General Non-Profit Corporation Laws of California, exclusively for religious, charitable, scientific, literary and educational purposes; no part of the net [24] earnings were to inure to the benefit of any private shareholder or individual and no substantial part of the activities of which was to carry on propaganda or otherwise attempt to influence legislation.

(b) In 1940 and 1941 Levi M. Davenport and his wife, Barbara N. Davenport, transferred or caused to be transferred to petitioner properties of a total value of \$270,384.00, in part consideration for which petitioner agreed to let the Davenports use one of the properties as their living place and agreed to pay over to the Davenports or to their daughter or granddaughter certain annuities, all of

which rights retained by the Davenports and assumed by petitioner had a value not in excess of \$90,315.38, with the result that petitioner received a net gift of at least \$180,068.62.

(c) Petitioner throughout its existence was and is a corporation organized and operating exclusively for religious, charitable, scientific, literary or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual and no substantial part of the activities of which is carrying on propaganda or otherwise attempting to influence legislation.

(d) Petitioner throughout its existence was a corporation organized for the exclusive purpose of holding title to property, collecting income therefrom and turning the entire amount thereof, less expenses, over to an organization which itself is exempt from the tax imposed by this chapter. [25]

(e) None of petitioner's net income was subject to income tax within the provisions of Section 101 (6), 101(14), 600, 1200 and 1201(a) (1) of the Internal Revenue Code for any of the years 1940 to 1944, inclusive.

Wherefore, petitioner prays that the Court may hear this proceeding and determine that petitioner is exempt from Federal corporate income and declared value excess profits tax for the years 1940 to 1944, inclusive.

/s/ MELVIN D. WILSON

/s/ REX DIBBLE

Counsel for Petitioner. [26]

State of California,  
County of Los Angeles—ss.

Fred A. Flora and J. E. Steinour, being duly sworn, depose and say that they are the Secretary and Treasurer of The Davenport Foundation and are duly authorized to verify the foregoing petition; that they have read the foregoing petition and are familiar with the statements contained therein and that the statements contained therein are true except those stated to me upon information and belief and that those they believe to be true.

/s/ FRED A. FLORA

/s/ J. E. STEINOUR

Subscribed and affirmed by Fred A. Flora before me this 19th day of February, 1947.

[Notarial Seal] GUY GIALARD GIACOPUZZI  
Notary Public in and for Said County and State.

My commission expires July 23, 1947.

Subscribed and affirmed by J. E. Steinour before me this 21 day of February, 1947.

[Notarial Seal] HELEN M. WILLIAMS  
Notary Public in and for Said County and State.

My commission expires July 21, 1950.

[Endorsed]: Filed Feb. 14, 1947. [27]

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[Title of Tax Court and Cause.]

ANSWER TO AMENDED PETITION

The Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of



Internal Revenue, for answer to the amended petition of the above-named taxpayer, admits and denies as follows:

1 and 2. Admits the allegations contained in paragraphs 1 and 2 of the amended petition.

3. Admits that the taxes in controversy are Federal corporate income and declared value excess profits taxes; denies the remainder of the allegations contained in paragraph 3 of the amended petition.

4 (a) and (b). Denies the allegations of error contained in subparagraphs (a) and (b) of paragraph 4 of the amended petition. [28]

5 (a) to (e) inclusive. Denies the allegations contained in subparagraphs (a) to (e) inclusive, of paragraph 5 of the amended petition.

6. Denies each and every allegation contained in the amended petition not hereinbefore specifically admitted or denied.

Wherefore, it is prayed that the determination of the Commissioner be approved.

/s/ J. P. WENCHEL, ECC

Chief Counsel, Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,

Division Counsel

EARL C. CROUTER,

E. A. TONJES,

Special Attorneys,

Bureau of Internal Revenue.

EAT/rng 2/26/47

[Endorsed]: Filed March 1, 1947. [29]

[Title of Tax Court and Cause.]

Petitioner, a non-profit corporation organized pursuant to a trust created in 1939 by Levi M. Davenport, is not exempt from tax under section 101 (6) and (14) of the Internal Revenue Code.

Melvin D. Wilson, Esq., and J. Rex Dibble, Esq., for the petitioner.

E. A. Tonjes, Esq., for the respondent.

## MEMORANDUM FINDINGS OF FACT AND OPINION

Leëch, Judge: This proceeding involves Federal income and declared value excess-profits tax deficiencies, as follows: [30]

Year	Income Tax	Declared Value Excess-Profits Tax
1940	\$ 468.02	
1941	1,415.13	\$409.20
1942	2,292.63	300.11
1943	2,272.00	86.30
1944	2,804.44	

The issue is whether petitioner is exempt from income and declared value excess-profits taxes under section 101 (6) and (14) of the Internal Revenue Code. The case was submitted on a stipulation of facts and oral testimony. The facts as stipulated are so found. Additional facts are found from the evidence.

## FINDINGS OF FACT

Petitioner is a corporation with its principal office at Pasadena, California. Its tax returns for the

periods involved were filed with the collector of internal revenue for the sixth California district.

On May 23, 1939, Levi M. Davenport executed an irrevocable transfer in trust of certain real and personal property to LaVerne College, a corporation, incorporated under Title XVII, Part IV, Division 1, Sections 649 to 651, Civil Code of the State of California, as trustee, and "C. Ernest Davis, Lucile Davenport Weller, J. E. Steinour, Fred A. Flora and L. E. Miller, constituting a board of directors." On the same day this board of directors adopted by-laws for the trust, called "The Davenport Foundation." On the date of the transfer such property had a value of \$261,884. On June 1, 1939, Barbara N. Davenport, wife of the donor, transferred to the trust two parcels of real estate having a value of \$8,500. [31]

The trust indenture states that the trustor is desirous of establishing a permanent foundation to be known as "The Davenport Foundation" for the purposes described therein. It provides that the only duty or obligation of the trustee shall be to hold title and perform such acts as shall be necessary to carry out the orders and directions of the board. The board shall act and constitute the board of trustees of the Foundation and shall have complete control, management and operation of the property forming the trust estate; shall receive and collect the principal and income and, after the payments and deductions hereinafter mentioned, shall pay and/or accumulate, and/or use and invest, hold, apply and distribute the same to, or for the purposes

hereinafter stated. No specific purposes are stated other than contained under certain designated headings. For instance, under the heading "Reserves" it provides:

Before distribution is made of any of the net income reserves shall be set aside as follows to wit:

- (1) 25% of the gross income for taxes, supervision and upkeep.
- (2) 12% of the gross income for replacements and betterments.

Under the heading, "Distribution of Income", it provides:

All the net income available for distribution shall be paid in monthly installments, as follows:

- (1) To the Trustor, Levi M. Davenport, the sum of Four Hundred Dollars (\$400.00) per month, for and during the term of his natural life.
- (2) To LaVerne College, a corporation, the sum of Three Hundred Dollars (\$300.00) per month for the purpose of establishing a department of Philosophy and Religion, which department shall be established at the beginning of the school year 1939-1940.
- (3) To make suitable and proper provision for the support and maintenance of J. R. Davenport, my brother, as his needs may require, not to exceed however, One Hundred Dollars (\$100.00) per month, all of



which shall be at the sole discretion of the Board of Trustees. In the event that any of my children shall come to want, the Board of Trustees shall use a portion of the income to care for them in so far as their needs may require, all of which shall also be solely within the discretion of the Board of Trustees.

- (4) To American Bible Society, with its principal office at Bible House, New York City, the sum of Three Hundred Dollars (\$300.00) per annum, payable annually at the discretion of the Board.
- (5) To the payment of annuities in such amounts as may be agreed upon between the Board of Trustees and the annuitants, who may add to this Trust.
- (6) All of the rest and residue of undistributed income shall be used by the Board of Trustees for such purposes consistant [sic] with the purposes of this trust as may be determined in the sole discretion of said Board of Trustees.

The trust indenture outlines in detail the courses to be given and taught by the Department of Philosophy and Religion and the general procedure to be adopted in teaching the subjects.

Under the heading "Reservations," the following provision is made:

It is understood and agreed that during the lifetime of the Trustor, Levi M. Davenport, that

the Trustor shall have the right to the use and occupation, rent free, of the home now occupied by him at 674 Elliot Drive, Pasadena, California, or some other home of similar rental value.

The trust indenture also contains provisions covering "Vacancies on Board of Trustees," "Compensation of Trustees," "Additions to the Foundation," "Change of Beneficiary" and "Powers of Trustees." There is a provision restricting each beneficiary from "anticipating, encumbering, alienating or in any other manner assigning his or her, or its interest" in either principal or income. After the death of the trustor and the individual beneficiaries, the board of trustees is authorized to incorporate the Foundation, in which event La Verne College shall convey all of its title in the trust estate to such corporation upon request of the board.

Included in the real estate conveyed to the trust by Levi M. Davenport was a parcel known as the "First Street property." After the trust was created the trustor desired to improve such property. The trustee was advised by its attorney that it could not borrow money for the benefit of the trust, but it could reconvey the property to the trustor, have him borrow the money and make the improvements and then reconvey it to the trust. This plan was followed.

It was agreed by the board of trustees and the trustor that the Davenport home, which had been conveyed to the trust, had been transferred to the trust by mistake and had not been intended to be

a part of the trust at that time. Accordingly, about March 26, 1940, the trustees reconveyed this property to the trustor.

On July 8, 1940, petitioner was incorporated under the laws of California as a non-profit corporation, for the stated purpose "To act as Trustee under Christian Educational, Charitable, Eleemosynary, and other charitable trusts." [34] Specifically, petitioner was to replace La Verne College as trustee of the trust created by Levi M. Davenport. Petitioner's charter contains the usual powers and customary provisions found in corporate charters of this character. Its by-laws provide for a board of trustees, the election of officers and prescribe their powers and duties. They contain no provision for the distribution of income.

On September 5, 1940, the Davenport Foundation (the trust) adopted a resolution which, after certain preambles not here important, reads as follows:

Now Therefore Be it resolved that LaVerne College be, and it is hereby instructed to convey to The Davenport Foundation, a corporation, all of the property and assets which LaVerne College now holds under the said Declaration of Trust. Such conveyances and transfers shall be made subject to that certain Declaration of Trust of May 23rd, 1939, designated The Davenport Foundation, an unincorporated association, and the acceptance thereof by this corporation known as The Davenport Foundation shall be a recognition of the fact that the assets so transferred are subject to and accepted by this cor-

poration, subject to the terms and provisions of said Declaration of Trust.

On or about October 8, 1940, LaVerne College transferred to petitioner all the real and personal property which it held under and by virtue of the trust created by Levi M. Davenport and Barbara N. Davenport, his wife.

On or about May 31, 1941, Levi M. Davenport and his wife transferred to petitioner the Davenport "home place." Contemporaneously therewith, petitioner and the transferors executed an annuity agreement whereby (a) the transferors retained the right to use the home place for their lives; (b) petitioner agreed to pay Lucile Davenport Weller, transferors' daughter, an annuity of \$100 per month, and upon her death to pay to her daughter, Dorothy Mae Weller, an annuity of \$100 per month. Petitioner's obligation to pay such annuities was absolute and not dependent upon whether petitioner had net income or net earnings. The annuity to Dorothy Mae Weller is to be reduced under certain conditions not now material. No rent was ever paid to petitioner with respect to such home place. The value of the home place on May 31, 1941, was \$15,500 and its fair rental value was \$1,500 per annum. The taxes and other expenses of upkeep, all of which were paid by petitioner, were as follows:

Year	Taxes	Other Expenses
1941	\$481.49	\$1,040.65
1942	324.60	1,050.32
1943	296.52	113.62
1944	380.19	519.24



On or about May 31, 1941, Levi M. Davenport and his wife transferred to petitioner the aforementioned First Street property. Contemporaneously with such transfer, petitioner and the transferors executed an annuity agreement whereby Levi M. Davenport reserved the net income from such property for his life and reserved the right to designate in writing, during his lifetime, the disposition of such net income for a period not to exceed 10 years after his death. No such designation of the income was made by Levi M. Davenport. The value of the First Street property on May 31, 1941 was \$40,000 and its fair rental value was \$5,400 per annum. Petitioner never received any income from such property. The taxes thereon for the years 1940 to 1944, inclusive, were paid by Levi M. Davenport. The expenses of upkeep, paid by petitioner, were as follows: [36]

Year	Expenses
1940	\$ 8.62
1941	0.00
1942	63.02
1943	350.70
1944	1,297.78

During the years 1940 to 1944, inclusive, petitioner made donations or contributions to certain organizations which have not been established as exempt from taxation under section 101 of the Internal Revenue Code, as follows:

	1940	1941	1942	1943	1944
Phillip's China Relief .....					\$150.00
Radio Gospel Hour.....				\$50.00	35.00
Flora, Evangelist .....				8.00	
United America Defense Committee.....		\$25.00			
National Voice (Includes California Voice) .....			\$15.00	15.00	35.00
W. N. Miles Radio Program.....					10.00
State Wide Committee, Higher Educa- tion .....					2.00
Los Angeles Times.....			24.50		
Democratic Club for Willkie, Los An- geles, California .....	\$14.18				
Jeffersonian Democrats, Los Angeles, California .....	10.00	25.00			
Republican Club, Los Angeles, Calif.....					25.00
Democratic Club, Los Angeles, Calif.....					25.00
Property Owners' Assn., Los Angeles, California .....	10.00	10.00	10.00	10.00	10.00
	<hr/> \$34.18	<hr/> \$60.00	<hr/> \$49.50	<hr/> \$83.00	<hr/> \$292.00

Petitioner paid to Lucile Weller and Homer Davenport the following amounts:

Year	Lucile Weller	Homer Davenport
1940	\$1,000	
1941	1,200	\$625.00
1942	1,200	
1943	1,200	
1944	1,200	

The payment of \$1,000 in 1940 to Lucile Weller and the payment of \$625 in 1941 to Homer Davenport were payments for the benefit of Levi M. Davenport in connection with his acquisition of certain shares of the capital stock of L. M. Davenport Company which were surrendered to him by Lucile Weller and Homer Davenport. The payments to

Lucile Weller during the years 1941 to 1944, inclusive, were made pursuant to the terms of the annuity agreement.

During the taxable period 1940 to 1944, the net income, as determined by the respondent, was as follows:

Year	Net Income
1940.....	\$ 3,151.61
1941.....	6,587.50
1942.....	8,886.04
1943.....	8,897.62
1944.....	10,961.62
	<hr/>
	\$38,484.39

During the period 1940 to 1944, inclusive, petitioner paid to organizations and institutions exempt under section 101 (6) an amount aggregating \$20,124.09.

During the taxable periods involved, petitioner was not exempt from taxation pursuant to the provisions of section 101 of the Internal Revenue Code.

## OPINION

The sole question submitted is whether petitioner is exempt from taxation upon its income by virtue of section 101 (6) and (14) of the Internal Revenue Code.<sup>1</sup> The respondent argues that petitioner is not

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<sup>1</sup>Sec. 101. Exemptions from Tax on corporations.

The following organizations shall be exempt from taxation under this chapter—

\* \* \* \* \*

(6) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educa-

exempt under section 101 (6), since a portion of its income could and actually did inure to the benefit of private individuals. Respondent further contends that petitioner is not exempt under section 101 (14), for the reason that some portion of its income was paid to individuals or corporations not themselves exempt from tax. The material facts are not in dispute. Petitioner, a nonprofit corporation, was organized to act as trustee under charitable trusts. The properties which Levi M. Davenport and his wife had transferred under an irrevocable declaration of trust, dated May 23, 1939, were conveyed to petitioner subject to the terms and provisions of such trust. The only purposes stated in the trust instrument were to collect the income and distribute or accumulate the same as therein specified. The sum of \$400 per month was to be paid to Levi M. Davenport, the trustor, during his life; \$300 per month was to be paid to LaVerne College to establish a Department of Philosophy and Religion; in the discretion of the trustees, suitable and proper provision was to be made for the support and maintenance

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tional purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation;

\* \* \* \* \*

(14) Corporations organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof, less expenses, to an organization which itself is exempt from the tax imposed by this chapter;



of J. R. Davenport, brother of the trustor, as his needs may require, not exceeding \$100 per month; in the event that any of the trustor's children should come to want, a portion of the income was to be used to care for them as their needs may require; \$300 per annum was to be paid to the American Bible Society; and the residue of the undistributed income was to be used for purposes consistent with the purposes of the trust. Obviously, the income of the trust was not to be devoted exclusively to charitable purposes. Nor were the purposes, other than charitable, merely incidental to the charitable purposes. *James Sprunt Benevolent Trust*, 20 B.T.A. 19; *Scholarship Endowment Foundation v. Nicholas*, 106 Fed. (2d) 552. The payments to be made to the trustor and the members of his family were at least equally the concern of the trustor. One of the dominant purposes for which the trust was created was those payments. The provision contained in the trust to the effect that the Foundation was not to be incorporated until after the death of the trustor and the other individual beneficiaries seems to confirm this view.

Petitioner contends that since the First Street property and the [40] home property were conveyed to petitioner subject to certain reserved interests and the payment of specific annuities, it falls within the rule of *Lederer v. Stockton*, 260 U. S. 3; *Emerit E. Baker, Inc.*, 40 B.T.A. 555. To these may be added the case of *Edward Orton, Jr. Ceramic Foundation*, 9 T.C. 533, decided since the filing of briefs herein. In *Lederer v. Stockton*, supra, the Supreme Court held that a hospital was not liable

for tax on income it had received from property devised to it but subject to the payment of annuities. In *Emerit E. Baker, Inc.*, supra, it was held that a corporation otherwise exempt from income tax under section 101 (6) of the Revenue Acts of 1934 and 1936 is not deprived of exemption because of payments to a donor's widow and of payment for the education of her nieces or nephews pursuant to the donor's will. The decision was based on *Lederer v. Stockton*, supra. In *Edward Orton, Jr. Ceramic Foundation*, supra, we held, under the rationale of the Baker and Lederer cases, that the Foundation was exempt from tax under the following facts: Edward Orton, Jr., deceased, by his will provided for the creation of a Foundation for aiding and promoting the science of ceramic engineering. He divided his estate into Parcel No. 1 comprised of a going business engaged in the manufacture of pyrometric cones, and Parcel No. 2, consisting of all the remaining assets of his estate. Since Parcel No. 1 contained the principal income producing properties, he directed the trustees controlling Parcel No. 1 to pay his widow the sum of \$42,000 over a period of five years. The widow, being the sole heir, had the election to [41] take under the will or under the Ohio statutes of distribution and descent which entitled her to a one-half interest in all the testator's property. She elected to take under the will, but as a condition to such election entered into a contract with the trustees whereby, after the completion of the payments of the sum of \$42,000 provided in the will, she was to be paid a life annuity of \$350 per month. The payments to the widow were a charge

upon all the assets of the Foundation. Of the sum of \$42,000, all had been paid prior to the taxable year except \$2,845.93. It was held that the Foundation was a separate distinct entity; that the payments to the widow were not the real purposes for which the Foundation was established, but were payments which had to be made to free the assets and income for use in the scientific aims of the Foundation. The instant case is readily distinguishable. If the First Street property and the home property which were transferred to petitioner, subject to reservations, were the only properties here involved, the similarity of the cases might prevent their distinguishment. The record here establishes that the First Street property and the home property were conveyed as a part of the original trust. Later, these properties were conveyed back to the trustor, and subsequently reconveyed to petitioner under certain reservations. The legality of such transactions may be somewhat doubtful since the original declaration of trust was by its terms irrevocable, and there is no evidence that the individual beneficiaries of the trust, other than the trustor, ever consented to such reconveyance. However, [42] we need not dwell on the legality of these retransfers to the trustor since additional properties were transferred under the original trust, the income from which was to be distributed to members of the trustor's family. And it does not appear that such beneficiaries ever waived or surrendered their rights under the original trust. The petitioner accepted these additional properties "subject to the terms and provisions of said Declaration of Trust."

Furthermore, this record shows that during the taxable periods a portion of petitioner's income was actually used to pay taxes and other expenses of the trustor's home and to provide an annuity of \$100 per month to trustor's daughter, Lucile Davenport Weller. Substantial sums were also paid for the upkeep of the First Street property. Since the trust was created for private as well as for public purposes, all the income of the trust corpus was not to be devoted exclusively to charitable purposes. To be classed as tax exempt under section 101 (6) of the Internal Revenue Code, a corporation must establish that no part of its income is to inure to the benefit of a private individual or stockholder. *James Sprunt Benevolent Trust, supra*; *Scholarship Endowment Foundation v. Nicholas, supra*. We conclude petitioner has not met the test prescribed in the statute.

Nor do we think petitioner qualifies as an exempt corporation under the provisions of section 101 (14) of the Code. In the taxable years a portion of petitioner's income was distributed to organizations or persons not exempt from tax. Out of its total income of \$38,484.39, [43] approximately \$20,000, only, was actually distributed to corporations or individuals properly classified as exempt from tax. To come within the purview of subdivision (14), a corporation must be organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof, less expenses, to an organization which itself is exempt from tax. Clearly,



petitioner does not meet this test. The respondent's determination is sustained.

Entered Dec. 24, 1947.

Decision will be entered for the respondent.

[Seal]

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The Tax Court of the United States  
Washington  
Docket No. 10427

THE DAVENPORT FOUNDATION,  
Petitioner,  
vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### DECISION

Pursuant to the determination of the Court, as set forth in its Memorandum Findings of Fact and Opinion, entered December 24, 1947, it is

Ordered and Decided: That there are deficiencies in tax, as follows:

Year	Income Tax	Declared Value Excess-Profits Tax
1940.....	\$ 468.02	\$ ———
1941.....	1,415.13	409.20
1942.....	2,292.63	300.11
1943.....	2,272.00	86.30
1944.....	2,804.44	————

Entered Dec. 29, 1947.

/s/ J. RUSSELL LEECH,  
Judge. [45]

[Title of Tax Court and Cause.]

PETITION TO REVIEW DECISION OF THE  
TAX COURT OF THE UNITED STATES

To the Honorable, the Judges of the United States  
Circuit Court of Appeals for the Ninth  
Circuit:

I.

Nature of the Controversy

Your petitioner, The Davenport Foundation, is a California corporation whose office and principal place of business is at 674 Elliott Drive, Pasadena, California.

On April 1, 1946, the petitioner filed with the Tax Court of the United States, pursuant to the provisions of the Internal Revenue Code, its petition requesting the redetermination of the deficiencies of corporation income and declared value excess profits taxes as shown by the official notice of deficiency mailed by the respondent under date of March 1, 1946, as follows: [46]

Year	Income Tax	Declared Value Excess Profits Tax
1940.....	\$ 468.02	\$ ——
1941.....	1,415.13	409.20
1942.....	2,292.63	300.11
1943.....	2,272.00	86.30
1944.....	2,804.44	——

The respondent filed his answer May 8, 1946, admitting the jurisdictional facts, but generally denying all of the other allegations of the petition.

On or about February 22, 1947, the petitioner filed an amended petition, having obtained permission from the Tax Court of the United States.

That the amended petition alleged that for the years 1940, 1941, 1942, 1943 and 1944 petitioner was a corporation organized and operated exclusively for religious, charitable, scientific, literary or educational purposes, no part of the net earnings of which inured to the benefit of any private shareholder or individual and no substantial part of the activities of which is carrying on propaganda or otherwise attempting to influence legislation and that petitioner was exempt from income tax under the provisions of Section 101(6) of the Internal Revenue Code and was exempt from declared value excess profits tax under the provisions of Sections 600, 1200, 1201(a)(1) of the Internal Revenue Code for the above specified years.

In the alternative, the amended petition alleged that petitioner was a corporation organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount [47] thereof, less expenses, to an organization which itself is exempt from the tax imposed by this chapter and hence petitioner was exempt for the years 1940 to 1944, inclusive, from income tax under the provisions of Section 101(14) of the Internal Revenue Code and exempt from declared value excess profits tax under the provisions of Section 600, 1200 and 1201(a)(1) of the Internal Revenue Code.

The respondent within the statutory time provided therefor filed his answer to the amended petition denying all the material allegations of the amended petition, excepting the jurisdictional facts.

On the 14th day of February, 1947, the cause was tried before Hon. J. Russell Leech, Judge of the Tax Court of the United States, sitting at Los Angeles, California. Petitioner filed its opening brief, respondent filed a brief and the petitioner filed a reply brief and the cause was submitted for decision. The Tax Court of the United States rendered its memorandum decision on December 24, 1947, and the final order of determination was duly entered on December 29, 1947, finding deficiencies as set forth above. [48]

## II.

### Designation of Court of Review

The petitioner being aggrieved by the said opinion, decision and order, desires a review thereof in accordance with the provisions of the Internal Revenue Code by the United States Circuit Court of Appeals for the Ninth Circuit, within which Circuit is located the office of the Collector of Internal Revenue to whom the said petitioner made its income tax returns for the years 1940, 1941, 1942, 1943 and 1944.

## III.

### Assignment of Errors

Now comes the petitioner, The Davenport Foundation, and assigns errors in the decision of the Tax Court of the United States as follows:

1. The Tax Court of the United States erred in failing to find that the petitioner was exempt from income and declared value excess profits tax for the years 1940 to 1944, inclusive, under the provisions of Section 101(6) of the Internal Revenue Code.



2. The Tax Court of the United States erred in finding that petitioner distributed \$100.00 per month of its income to grantor's daughter, Lucile Davenport Weller. [49]

3. The Tax Court of the United States erred in failing to make a requested finding that petitioner took property subject to an annuity of \$100.00 per month reserved by the grantor for the benefit of his daughter and granddaughter.

4. The Tax Court of the United States erred in finding that petitioner was required to distribute income to members of the grantor's family.

5. The Tax Court of the United States erred in failing to find that petitioner's predecessor received property subject to a discretionary liability to pay certain amounts to the members of the grantor's family.

6. The Tax Court of the United States erred in failing to find that upon the organization of petitioner, the discretionary liability of petitioner's predecessor trust to pay amounts to members of the grantor's family, was terminated.

7. The Tax Court of the United States erred in failing to find that the members of the grantor's family were in such good financial condition that it was extremely remote that they would ever be in actual want or request payments from petitioner.

8. The Tax Court of the United States erred in finding that petitioner, in paying taxes and maintenance expenses of the Davenport home, which belonged to petitioner, was distributing some of petitioner's income to the grantor.

9. The Tax Court of the United States erred in failing to find that any improper payments made by petitioner through its manager, Levi M. Davenport, for the upkeep of the Davenport home or for the First Street property or for unauthorized contributions will be recouped by petitioner through reduction of amounts owing by petitioner to Levi M. Davenport, or by claims against his estate.

10. The Tax Court of the United States erred in failing to find that the reservation by Levi M. Davenport of the income from the First Street property was in lieu of the provisions in the original trust indenture of the reservation by him of \$400.00 per month.

11. The Tax Court of the United States erred in finding that the \$1,000.00 petitioner paid to Lucile Davenport Weller and the \$625.00 it paid to Homer Davenport were distributions of petitioner's' income to private persons.

12. The Tax Court of the United States erred in failing to find that petitioner took property of Levi M. Davenport and Barbara M. Davenport subject to the amounts of \$1,000.00 and \$625.00 payable respectively to Lucile Davenport Weller and to Homer Davenport.

13. The Tax Court of the United States erred in finding that petitioner's income was not to be devoted exclusively to charitable and educational purposes.

14. The Tax Court of the United States erred in finding that the provisions for the grantors and their family was more than incidental to the main

purpose of petitioner as a charitable, religious and educational organization.

15. The Tax Court of the United States erred in failing to find that the payments by petitioner to Phillips China Relief and to the Radio Gospel Hour and to Flora, Evangelist, were amounts spent for religious, charitable and educational work.

16. The Tax Court of the United States erred in failing to find that petitioner never paid any of the \$400.00 monthly payments provided in the original trust indenture to or for the use of the grantor, Levi M. Davenport.

17. The Tax Court of the United States erred in failing to find that the payments made by petitioner to the Property Owners Association were deductible as an ordinary and necessary expense.

18. The Tax Court of the United States erred in failing to find that petitioner was exempt from income and declared value excess profits taxes for the years 1940 to 1944, inclusive, under the provisions of Section 101(14) of the Internal Revenue Code.

19. The Tax Court of the United States erred in holding that petitioner distributed some of its income to organizations or persons not exempt from tax.

20. The Tax Court of the United States erred in holding that petitioner was not exempt under Section 101(14) because it did not distribute, during the taxable years, the entire amount of its income.

21. The Tax Court of the United States erred in rendering decision for respondent.

Wherefore, petitioner prays that said errors be corrected and the judgment and findings of said Tax Court be reversed.

/s/ MELVIN D. WILSON,  
819 Title Insurance Building, Los Angeles 13, California, Counsel for Petitioner. [53]

State of California,  
County of Los Angeles—ss.

I, Melvin D. Wilson, state that I am one of the petitioner's attorneys of record in the above-entitled matter and am thoroughly familiar with the facts involved in said matter; that I have read said attached petition for review; that it closely states the facts, the matter in controversy and the history of the case, to the best of my knowledge and belief.

/s/ MELVIN D. WILSON.

Subscribed and Sworn to before me this 15th day of March, 1948.

[Seal] /s/ NORMA LUND,

Notary Public in and for Said  
County and State.

My Commission Expires August 8, 1949.

[Endorsed]: Filed March 24, 1948. [54]



[Title of Tax Court and Cause.]

NOTICE OF FILING PETITION TO REVIEW  
DECISION OF THE TAX COURT OF THE  
UNITED STATES

To: Commissioner of Internal Revenue, Internal Revenue Building, Washington, D. C.; Charles Oliphant, Attorney for Respondent, Chief Counsel, Bureau of Internal Revenue, Washington, D. C.

You are hereby notified that on the 24th day of March, 1948, a petition for review by the United States Circuit Court of Appeals for the Ninth Circuit of the decision of the Tax Court of the United States heretofore rendered in the above-entitled cause, was filed with the Clerk of the Tax Court of the United States. A copy of the petition as filed is attached hereto and served upon you.

Dated March 24, 1948.

/s/ MELVIN D. WILSON,

Attorney for Petitioner, 819 Title Insurance Building, Los Angeles 13, California.

Service of the foregoing Notice of Filing and of a copy of the petition for review is hereby acknowledged this 24th day of March, 1948.

/s/ CHARLES OLIPHANT, CAR

Attorney for Respondent, Chief Counsel, Bureau of Internal Revenue.

[Endorsed]: Filed March 24, 1948. [55]

[Title of Tax Court and Cause.]

### STATEMENT OF EVIDENCE

The above-entitled cause came on for hearing at Los Angeles, California, before the Honorable J. Russell Leech, Judge of the Tax Court of the United States, upon the 14th day of February, 1947; Melvin D. Wilson and Rex Dibble, Esqs., appeared on behalf of petitioner, and E. A. Tonjes, Esq., appeared on behalf of respondent. Thereupon the following proceedings were had and the parties by their attorneys submitted the following evidence.

#### JOSEPH A. ALLARD, JR.

having been first duly sworn as a witness on behalf of the petitioner, testified as follows:

My name is Joseph A. Allard, Jr. I am an attorney at law. I have known Levi M. Davenport since 1932 or 1933 and I helped him work out the details of The Davenport Foundation. [56]

Mr. Davenport at the time of creating petitioner's predecessor, the trust called The Davenport Foundation, furnished me with deeds and policies of title insurance covering the various properties that he desired to transfer to the trust. Included among these was a deed to the Davenport home. I prepared deeds covering all the properties described by the deeds which he gave me and title to the Davenport home was transferred to the trust. Later Mr. Davenport called my attention to the fact that by mistake the home had been included, that it was not his intention to convey the home because he

(Testimony of Joseph A. Allard, Jr.)

had some matters to work out with his daughter, Lucile Davenport Weller, and until he had worked out these problems with her he wanted to retain the home; that he had given each of his two sons about \$35,000.00 but had given his daughter much less than that. For that reason he wanted the home back until he got her "inheritance," as he put it, worked out.

On my advice the LaVerne College, which held the title, conveyed the home place back to Mr. Davenport on the theory that it had been conveyed to the College by mistake. [57]

Q. Our stipulation shows that the home eventually went to the corporation, with the contract providing for an annuity for Mrs. Weller. Is that the definite arrangement that he finally made?

A. Yes. He talked with Mrs. Weller \* \* \* and he proposed to give her the home, provided she would agree to live in it as long as she lived, and she wouldn't accept it under those conditions, so then he suggested—or, requested that I prepare a simple annuity contract, whereby he would convey this property back into the Foundation, and provide that the Foundation would pay her, as an annuity, \$100.00 a month as long as she lived. The boys had had theirs for some time. This plan, he felt, would equalize, even though she lived long enough to get more than they actually received. They had had the benefit of what he gave them, but she had not had the benefit of very much, and he felt that would equalize it.

(Testimony of Joseph A. Allard, Jr.)

The property was reconveyed to the Foundation under an annuity agreement to pay his daughter Lucile \$100.00 a month during her lifetime. He had in mind that if each one of his children received a total of \$35,000.00 from him, that that would constitute their inheritance, which he expected to give them during his lifetime, and that everything else he had should go back into the work of God. It was very clear to me, from what he said to me, that it was his desire that eventually all of his property should go for this work after he had taken care of his children to the extent of \$35,000.00 apiece. [58]

Q. Mr. Allard, in the deed of the home to the petitioner, the use of it is reserved to the Davenports, but nothing is stated in the deed about the purpose or the use the corporation was to make of it after their lives had ceased.

Did Mr. Davenport say that the petitioner was to use the home after their deaths, for the purposes set out in the trust?

A. Yes, that was the intent, that this was to be part of the trust when their lives had terminated, and that the home should become part of the property to be used, the same as the other property was to be used, subject, of course, to the annuity to his daughter.

Some time after the First Street Property had been transferred to La Verne College, who held it as trustee under the original trust, which was not incorporated, Mr. Davenport desired to improve



(Testimony of Joseph A. Allard, Jr.)

the property, and my recollection is that he needed \$15,000.00 for the purpose of putting the improvements on the land. As attorney for the College, I was asked if they had the right to pledge their credit to borrow money for this purpose, and I said they did not. I suggested that the property be transferred back to Mr. Davenport, who [59] might borrow the money, sign the mortgage and then reconvey the property to the Foundation subject to the mortgage, and that procedure was followed. When in 1941 Mr. Davenport conveyed the First Street property over to petitioner, The Davenport Foundation, a corporation, he reserved the right to its net income for life and the right to appoint its net income for ten years after his death. In consideration therefor he gave up the right he had in the original trust indenture to receive \$400.00 per month for life.

“Q. In the original trust he gave the trustees discretionary right to help support his brother and children in need. Were these provisions cut off by the 1941 transfer of the First Street property to the petitioner?

“Mr. Tonjes: I object to the question, your Honor, on the ground that it calls for a conclusion of the witness, and that the documents speak for themselves as to what reservations were made.

“The Court: That objection seems sound.

“What is your answer?

“What the instrument does would certainly be proved by the instrument itself, not by what the witness thinks it does. [60]

(Testimony of Joseph A. Allard, Jr.)

“Mr. Wilson: Your Honor, the instrument does not say, but I think this witness can testify to other writings which indicated that it was to be cut off.

“The Court: Don’t you agree that, as to whether or not anything was retained, or what was retained by a particular instrument, is controlled by that instrument?

“Mr. Wilson: Not necessarily, your Honor.

“The Court: What is your position in this case?

“Mr. Wilson: Our position is that the provision in the original trust, that the trustees could assist his brother and his children, was that it cut off when the corporation was formed, and Mr. Davenport retained the right to appoint the income from the First Street property for ten years after his life.

“The Court: Your position is that that was the effect of the first instrument?

“Mr. Wilson: It was one of the purposes of forming the corporation and of making the general agreement with respect to the First Street property.

“The Court: You now ask this witness what? What is the question, please?

“Mr. Wilson: If it was the understanding between Mr. Davenport and the corporation that the provision [61] in the trust that the trustees could give some assistance to his brother and children was cut off by the provision by which he could appoint the income from the First Street property for ten years after his death.

(Testimony of Joseph A. Allard, Jr.)

“The Court: As we understand, the respondent’s objection is that this is in effect varying the terms of a written instrument, or might be, and that is the purpose for which it is offered.

“As we understand, the rule of this Court is that since the parties to the instrument are not in the dispute, one on either side, but that the government is on one side and the agreement on the other, that that rule does not apply. That is the rule of this Court, with which this division does not agree, but that is the rule of this Court now.

“That being so, we overrule the objection, note an exception to the respondent, but caution the witness again that we do not want his opinion as to what the understanding was, that is, what was in the mind of the individual and what was in the mind of the executive officers of the corporation, but what was said by either or both of them having to do with that. [62]

“The Witness: Your Honor, my conversations were with Mr. Davenport. I don’t recall that I had any in this regard with any of the officers of the corporation, and, at the time that the corporation was organized, it was done for two specific purposes, according to what he said to me that he wanted done.

“First, I might say that I told Mr. Davenport that I was not familiar with these matters of tax exemption, that I wouldn’t take any responsibility for the status of the corporation with respect to its

(Testimony of Joseph A. Allard, Jr.)

tax exemption, and he should consult tax counsel on that point, and he told me he had. It wasn't Mr. Wilson, however.

"He said he wanted this corporation formed for two reasons.

"First: When he first tried to borrow money on the First Street property, he found he was in difficulty, and, this being a real estate corporation, there had been constant transactions of sales and borrowing money for improvement, and that sort of thing, and he wanted to have it fixed up so it would be more simple. That was one thing.

"But, the other thing was that he wanted to get rid of all of these provisions in the original trust agreement whereby income went to individuals, because by [63] that time he had become concerned over the exempt status of the trust, because of certain income, by its provisions, going to individuals.

"So, for two reasons, he wanted the corporation formed; first, to make it more easy to borrow money and do business, and, secondly, to eliminate the income to the individuals, and that he would take care of his children in other ways, and I know that he tried to do that shortly before his death, but did not accomplish his purpose fully."

Q. (By Mr. Wilson): Mr. Allard, are you counsel for The Davenport Foundation?

A. Well, I don't know just exactly how to answer that. Sometimes they consult me, and sometimes others have been consulted, and Mr. Davenport, as you know, operated the Foundation practically as a one-man proposition in his lifetime. He



(Testimony of Joseph A. Allard, Jr.)

had some attorney in Los Angeles with whom he consulted, and he consulted with me, and the board have consulted me about some of their problems.

Q. Did you draw the instrument by which the First Street Property was transferred to Petitioner?

A. I am very certain that I did, Mr. Wilson.

Q. And the contract providing that he would get the net income for life? A. Yes. [64]

### Cross-Examination

By E. A. Tonjes:

After the First Street property was transferred to the petitioner, there were no more rights in any of the brothers or children of Mr. Davenport to obtain any payments from the corporation. That was part of the reason why Mr. Davenport wanted this corporation formed. I did not have any discussion with the brothers or children about this and did not get from them any writing or release of any rights they might have had in the property or to receive its income. All my discussions concerning this were with Mr. Davenport.

### J. E. STEINOUR

having been first duly sworn as a witness on behalf of the petitioner, testified as [65] follows:

My name is J. E. Steinour. Just now I am running a factory. I have been a pastor—a minister of a church. I knew Levi M. Davenport. I am a trustee and the Treasurer of petitioner. I knew Mr. Davenport very well during his lifetime.

(Testimony of J. E. Steinour.)

I do not have any knowledge of any assignments of income made by Barbara N. Davenport during her life of property she transferred to petitioner. To the best of my knowledge no such transfer was made. She left no will.

Levi M. Davenport during his lifetime did not serve upon petitioner any notice or document indicating that he had assigned to other persons, to take effect at his death, the income from the First Street property. Two weeks before his decease he told me that he had made no assignment.

“Q. Did Mr. Davenport ever speak to you about the effect of the forming of the corporation, and the 1941 agreements relating to an annuity for his daughter, and the right to assign income to the First Street property, as having any effect on the provisions of the original trust, making some allowances for his brother and children? [66]

“Mr. Tonjes: I object to that as being wholly immaterial, your Honor. The rights of the parties, I think, are all fixed by the documents which are attached to the stipulation, and what discussion Mr. Davenport had with Mr. Steinour regarding these rights I think is wholly immaterial. I don't know what petitioner is expecting to prove by it. Maybe we can inquire into that.

“Mr. Wilson: The same thing I was after with Mr. Allard, to show that the provisions of the trust have been cut off, which provisions were for the benefit of his brother and children—they have been

(Testimony of J. E. Steinour.)

cut off by more specific arrangements made in 1941, after the corporation was formed.

“The Court: Specific arrangements between whom?

“Mr. Wilson: Mr. Davenport and the corporation, to take care of his brother and children, or anyone.

“The Court: How would you go about proving that? Do you mean to say that those arrangements were oral or in writing?

“Mr. Wilson: They were in writing.

“The Court: Wouldn't the best evidence of that be in the writing, then? [67]

“Mr. Wilson: They are the two writings. We think the one replaces the other, but they do not say so expressly. We think that was the intention and the effect.

“The Court: We are a little at a loss to see what the picture is here.

“You are now trying to show the effect, as we understand it, of an agreement here that is not incorporated in either of the agreements in evidence.

“Mr. Wilson: That is about it, that the second agreements cut off the first.

“The Court: And you propose to show that how, now? You said, as we understand, a moment ago, that the agreements—one was intended to cut off the other, to be substituted for the other, and that that agreement was in writing. Did you mean that?

(Testimony of J. E. Steinour.)

“Mr. Wilson: The statement of cutting off is not in writing. They were simply the two agreements, and we want to show that the second one was to be in lieu of the other one.

“The Court: And you propose to show that how?

“Mr. Wilson: By showing that that was the understanding and intention between Mr. Davenport and the corporation. [68]

“The Court: In conformity with what we understand our rule to be, we overrule the objection, note an exception, and direct the witness not to state what the understanding was, but what was said by Mr. Davenport on the one hand, or by the officers of the corporation on the other, from which a conclusion would be proper, but the conclusion will be for us to make, not for the witness to make.

“Mr. Tonjes: Your Honor, might I be heard briefly at the moment?

“The Court: You may.

“Mr. Tonjes: I do not understand the proposition exactly in that light. I gather from what Mr. Wilson said that he expects this witness to place an interpretation upon the effect of the second document.

“The Court: We did not so understand that.

“Mr. Wilson: Yes.

“The Court: Objection sustained. Exception to the petitioner.”

Petitioner has never paid to Mr. Levi M. Davenport the \$400.00 per month that is provided for in the original trust indenture. He received the earn-



(Testimony of J. E. Steinour.)

ings of [69] the First Street property in lieu of the \$400.00 per month. That was Mr. Davenport's intention according to his discussion with me. Mr. Davenport in transferring the First Street property back to petitioner in 1941 reserved the right to appoint the income from that property for 10 years after his death. He made this reservation so he could assign the earnings after his death for the benefit of his brother and children if he wanted to, but he made other arrangements. I cannot recall that Mr. Davenport ever stated that the right to appoint the income from the First Street property was to be in lieu of the provision of the original trust for some care of his brother and children.

Mr. Davenport managed petitioner up to the time of his death. He was the general manager of petitioner.

The remaining trustees are, since the death of Mr. Davenport, making some investigation of the books and records of petitioner. If we find any expenditures, made under the management of Mr. Davenport, which the Board of Directors and trustees of petitioner think are improper, we propose to make a claim against Mr. Davenport's estate for such amount, or to offset the debt which petitioner owed to Mr. Davenport at the date of his death.

The Phillips China Relief is an independent missionary organization. After the witness so testified, Mr. Tonjes, attorney for the government, objected to the question on the ground that the witness had not been shown to be qualified.

(Testimony of J. E. Steinour.)

“The Court: He of course knows that he is testifying only from personal knowledge. Objection overruled. Exception to the respondent.

“Mr. Tonjes: Very well.

“The Witness: I telephoned to Mr. Phillips, got his wife, this morning, and asked if they were exempt, tax exempt. She said they were.”

Mr. Phillips is a preacher. He uses the contributions for China relief. He gets contributions from the public generally and sends it for China relief.

The Property Owners Association of Los Angeles, California, is an organization that looks after taxable conditions of property and so on. It assists taxpayers in keeping down the local taxes. Petitioner made contributions of \$10.00 per year to that organization for the purpose of trying to keep down the taxes on its property. [71]

#### Cross-Examination

By E. A. Tonjes:

The sum of \$400.00 a month, which was to be paid to Mr. Davenport, was never paid.

Q. Do you know why it was never paid?

A. Well, up to the time of the new arrangement with the First Street Property, that he was actually giving his time as manager.

I had some discussions with Mr. Davenport concerning the \$400.00 per month to the effect that he had organized this corporation, not for profit, but it was a matter of giving away his services and his money for a righteous cause, and so he did not need

(Testimony of J. E. Steinour.)

this \$400.00, and he never drew it, up to the time of the new arrangement, and then it was worked through the First Street Property. The \$400.00 a month which we have been referring to, was provided for in a written instrument. When Mr. Davenport and I had these discussions, we both recognized that Mr. Davenport had a right to the \$400.00 a month until the new setup with the First Street Property. This was in lieu of the other. I was on the board and had a very close relationship with him. The general nature of the circumstance whereby Mr. Davenport did not receive the \$400.00 a month was that he waived the payment of it. He had a right to receive it under the first arrangement.

I got the address of the Phillips China Relief out of the telephone directory. I telephoned out there and [72] talked to Mrs. Phillips. She said that her husband would not be back until that afternoon, that he had gone away, and that the funds that had been collected had been used for the purpose that they were given for, for China relief, that they were an independent missionary organization, and were tax exempt. That is all I know about it. I didn't examine their charts. I do not know whether they were an incorporated organization.

#### Redirect Examination

By Mr. Wilson:

Q. Did you consider that Mr. Davenport had the right to get the \$400.00 a month under the original

(Testimony of J. E. Steinour.)

trust indenture after the new agreement in 1941 with the petitioner?

A. No. This last was in lieu—it was in lieu of the former.

### Recross-Examination

By E. A. Tonjes:

I don't know whether or not there was any writing to that effect. I know of none. But I may say this, that the fact of his never drawing any money would indicate that this last arrangement superseded the other one.

### MRS. LUCILE WELLER

having been first duly sworn as a witness on behalf of the petitioner, testified as follows: [73]

My name is Mrs. Lucile Weller. I am a daughter of Levi M. Davenport. Many years ago some stock of the L. M. Davenport Company was issued to me and to my brothers. The L. M. Davenport Company was liquidated about the time my father organized The Davenport Foundation. I received a check for \$1,000.00 from my father on account of the stock I had in the L. M. Davenport Company.

Q. Were you a stockholder of L. M. Davenport Company when it liquidated?

A. I guess so, if I held the certificate.

Q. Did you get any of its assets?

A. He cashed this stockholder's certificate for me, just before he began giving me \$600.00 a month on my annuity, which started January 1, 1941.



(Testimony of Mrs. Lucile Weller.)

The Court: Well, do you know what happened? You got some money. From whom did you get it? Where did it come from?

The Witness: I got one thousand dollars.

The Court: From whom?

The Witness: On this certificate, from my father, and he paid me checks, and I didn't pay any attention whether they were Davenport Foundation checks or whether they were his personal checks, because he had both accounts, but I certainly know where that money came from. [74]

The Court: Where did it come from?

The Witness: It came from my father.

I do not know about any appointment my father may have made with respect to the income of the First Street property to take effect after his death.

I have one child—a daughter—who is a professional woman and is not dependent upon me. I have a husband and he is able-bodied. The combined income of my husband and myself is more than enough to take care of us so we have had enough to share with others. I am not worried about the future. My daughter is a high school teacher and receives a salary of \$240.00 or \$250.00 a month. She is married and her husband is working at his doctor's degree at the university and he receives a school allowance from the federal government.

The assets of my husband and myself are worth from \$85,000.00 to \$100,000.00. My husband is [75] employed as an insurance salesman. He is a retired agriculturist and has just recently gone into the insurance business.

(Testimony of Mrs. Lucile Weller.)

Barbara N. Davenport, the wife of Levi M. Davenport, died in November, 1943.

My brother, Ralph Davenport, has an important position with the gas company. He receives a very good salary and has a responsible position on the West Coast. He does not have a large family. He lives in a large house and has a high standard of living.

The Court: What do you mean by gets a very good salary?

The Witness: I couldn't tell you what it was, but he has a responsible position.

Q. (By Mr. Wilson): Would you say \$20,000.00 a year? Would you guess it was \$20,000.00 a year?

A. I don't know. I couldn't say. [76]

#### Cross-Examination

By E. A. Tonjes:

My father gave me some stock in the L. M. Davenport Company when I was very young, probably a certificate for 10 shares at \$100.00 per share. I held the stock from approximately 1922 until I turned it back to him at his request. I considered myself the owner of that certificate all of those years. I did not receive any dividends on it. I got the \$1,000.00 about the time he dissolved the L. M. Davenport Company and formed The Davenport Foundation. I don't know whether I turned it back to my father as an individual or to the corporation. I do not know how much the stock was worth but I got [77] \$1,000.00 for it.

(Testimony of Mrs. Lucile Weller.)

In 1941 my daughter was teaching and got her salary of \$250.00 a month and my husband was a farmer. We had a comfortable income from rental property in Los Angeles. I sold one of our properties about that time and put the money out at interest. My personal income would be around about \$100.00 per month in 1941. I cannot tell what our income was in 1942, 1943 or 1944. We were farming and during these war years farmers' income was very comfortable.

### HOMER H. DAVENPORT

having been first duly sworn as a witness on behalf of the petitioner, testified as follows:

My name is Homer H. Davenport. I am a son of Levi M. Davenport. In 1941 The Davenport Foundation paid to me \$625.00 for the 10 shares of the L. M. Davenport Company which I had. The L. M. Davenport Company has been dissolved and I was a stockholder at the date of dissolution. I did not get a share of the assets which amounted to \$400,000.00 to \$500,000.00, including real estate. All of the real estate that came from the L. M. Davenport Company went into The Davenport Foundation. The Davenport [78] Foundation, the petitioner, paid me the \$625.00 because the L. M. Davenport Company had just been dissolved and this was my share of the assets.

I have no knowledge that L. M. Davenport prior to his death made any assignment or appointment to take effect after his death of the income from the

(Testimony of Homer H. Davenport.)

First Street property. I do not know anything about the affairs of Barbara N. Davenport at all.

I have two pieces of property, one worth about \$12,000.00 and the other one about \$10,500.00. I owe a few thousand dollars on them. In addition, I have a half interest in a piece of property on Fourth Street. The value of my half interest is \$14,000.00. It produces an income of about \$260.00 a month which is used up in paying off the loans. The loan against said property is about \$5,000.00. I am not employed and I am not engaged in business. I have been in very poor health.

#### Cross-Examination

By E. A. Tonjes:

In 1940 my income was between \$1,600.00 and \$1,700.00. In 1941 it was approximately the same, also in 1942. In 1943 it was probably \$3,500.00, also for 1944. I am married and have no children. My wife has no independent [79] income. I do not think I could estimate my net worth in the years 1940 to 1944.

#### JOHN R. DAVENPORT

having been first duly sworn as a witness on behalf of petitioner, testified as follows:

My name is John R. Davenport. I am a brother of Levi M. Davenport. I have no knowledge of any appointment by Levi M. Davenport during his life to take effect after his death of any of the income from the First Street property.



(Testimony of John R. Davenport.)

I have property worth \$18,000.00 to \$20,000.00 net. I get about \$200.00 a month from it. I do not have any children or dependents. I am 71 years of age. My property is sufficient to keep me.

### Cross-Examination

By E. A. Tonjes:

In 1940 I worked and had an income of about \$250.00 per month and also in 1941 and 1942 and until August of 1943 when I quit. In addition, I had my property income. I would estimate that my total income for the years 1941, 1942 and 1943 was between \$4,000.00 and \$5,000.00 per year until I quit working in 1943 after which it was about \$3,500.00 per year.

In 1940 I estimate that I was worth about \$8,000.00 and about the same in 1941, also in 1942. In 1943 I was probably worth \$12,000.00 to \$14,000.00 and in 1944 it had gone up to \$15,000.00.

### FRED A. FLORA

having first affirmed as a witness on behalf of the petitioner, testified as follows:

My name is Fred A. Flora. I am a minister—a pastor of a church. I am the Secretary of The Davenport Foundation, the petitioner, also one of the Directors, and have been since the organization.

The National Voice is a temperance paper passing out temperance information.

(Testimony of Fred A. Flora.)

The Radio Gospel Hour, Dr. M. H. Fagan, is a minister. I know him well. He ministers in the Country Church of Hollywood and carries on a radio program. This is a faith work, as I understand it, supported by the free gifts of the folks who listen. His radio program is dependent on the support of the listening public. He represents that the contributions will be used solely for that purpose. [81]

In 1943 The Davenport Foundation, the petitioner, made a payment on its books called "Flora, Evangelist." This was not a personal contribution to me but it was given at a meeting in my church when we were having a special meeting promoting religious things and was given in an offering. It did not accrue to me personally but went to the carrying on of the church work. Contributions to the church of which I am a pastor are for religious and charitable work.

#### Cross-Examination

By E. A. Tonjes:

As a director of The Davenport Foundation I did not participate in a discussion of the contributions to be made by that corporation. Mr. Davenport was the founder of it and he directed where the contributions were to be made and I was not particularly consulted with reference to them.

## MRS. ELIZABETH CRIPPEN

having been first duly sworn as a witness on behalf of the petitioner, testified as follows:

My name is Mrs. Elizabeth Crippen. I am a certified public accountant. I have audited and kept the [82] books of The Davenport Foundation, the petitioner, for the last several years.

The Davenport Foundation has not entered on its books any rent received from Mr. or Mrs. Davenport for their use of the Davenport home.

## Cross-Examination

By E. A. Tonjes:

The Davenport Foundation, the petitioner, paid out taxes and certain amounts of other expenses on the Davenport home for the years 1941 to 1944.

Thereupon upon the joint motion of the petitioner and the respondent there was introduced into evidence the following exhibits which are made a part of this statement of evidence:

Joint Exhibit 1-A—copy of declaration of trust. Attached to the declaration of trust was Schedule A which described all the real and personal property which constituted the trust corpus and which Levi M. Davenport and Barbara N. Davenport transferred and conveyed to The Davenport Foundation on May 23, 1939. The description of said property is not considered necessary for the purpose of this record except to state that it included the "Davenport home," and the "First Street prop-

erty." The [83] by-laws of the trust called The Davenport Foundation, are a part of Joint Exhibit 1-A.

Joint Exhibit 2-B—deed dated June 1, 1939, from Barbara N. Davenport and Levi M. Davenport to LaVerne College. This was an outright deed of property which had belonged to Barbara N. Davenport. Not considered necessary to print the deed in this statement of evidence.

Joint Exhibit 3-C—deed dated June 1, 1939, from Barbara N. Davenport to LaVerne College. [84]

This was an outright deed of property which had belonged to Barbara N. Davenport. Not considered necessary to print the deed in this statement of evidence.

Joint Exhibit 4-D—agreement dated June 1, 1939, between Barbara N. Davenport and LaVerne College for the use of the property covered by Joint Exhibits 2-B and 3-C and the reservation from such transfers.

Joint Exhibit 5-E—copy of deed from LaVerne College to L. M. Davenport of the First Street property. Also copy of the resolution of the executive committee of the Board of Trustees of LaVerne College authorizing said transfer. Descriptions and acknowledgment omitted from both exhibits.

Joint Exhibit 6-F—copy of resolution of the Board of Directors of the trust making a request of LaVerne College that it deed the First Street property to Levi M. Davenport for certain purposes. Description omitted. [85]



Joint Exhibit 7-G—copy of deed dated March 26, 1940, from LaVerne College to Levi M. Davenport of the Davenport home. Description and acknowledgment omitted.

Joint Exhibit 8-H—copy of the articles of incorporation of The Davenport Foundation, petitioner. The corporation was formed July 8, 1940, under Title XII, Article 1 of the General Non-Profit Corporation Law of the State of California.

Joint Exhibit 9-I—copy of the by-laws of The Davenport Foundation, petitioner, adopted September 5, 1940. [86]

Joint Exhibit 10-J—copy of resolution adopted by the Board of Directors of the trust on September 5, 1940, requesting LaVerne College, trustee, to deed the property which it had on hand and had received from Levi M. Davenport and Barbara N. Davenport to petitioner, The Davenport [87] Foundation, a corporation.

Joint Exhibits 11-K and 12-L—copies of deeds from LaVerne College to the petitioner of properties which had been received from Levi M. Davenport and Barbara N. Davenport or acquired in exchange therefor or purchased from the proceeds thereof. Descriptions and acknowledgments omitted. It was stipulated that LaVerne College also transferred to the Davenport Foundation, petitioner, on or about October 8, 1940, any and all personal property it held as trustee and which it had received from Levi M. Davenport or Barbara N. Davenport.

Joint Exhibit 13-M—copy of deed dated May 31, 1941, from Levi M. Davenport and Barbara N. Davenport of the Davenport home to petitioner. Description and acknowledgment omitted.

Joint Exhibit 14-N—copy of an agreement dated June 23, 1941, between petitioner and Levi M. Davenport and Barbara N. Davenport relative to the Davenport home which was in effect until the date of the death of said natural persons.

Joint Exhibit 15-O—copy of a deed dated May 31, 1941, from Levi M. Davenport and Barbara N. Davenport to petitioner of the First Street property. Description and acknowledgment omitted.

Joint Exhibit 16-P—copy of agreement dated June 23, 1941, between petitioner and Levi M. Davenport and Barbara N. Davenport relative to the First Street property.

Joint Exhibit 17-Q—a statement of the taxable net income, per Revenue Agent's Report, and the book net income of petitioner for the period July 1, 1940, to December 31, 1944; also statement of the amounts paid to Lucile Weller under the agreement of June 23, 1941, being Joint Exhibit 14-N.

It was stipulated between the parties that the properties, real and personal, involved in the transfer by Levi M. Davenport to the trust, The Davenport Foundation, and from the trust to petitioner or directly from Levi M. Davenport to petitioner were valued at the dates of transfers, at \$261,-884.00.

It was further stipulated that the names and birth dates of Levi M. Davenport's closest relatives are as follows: [89]

Name	Birthdate
Levi M. Davenport.....	8/ 4/61
Barbara N. Davenport (wife).....	10/28/67
Lucile D. Weller (daughter).....	5/20/93
Dorothy M. Weller Halverstock (granddaughter).....	11/22/22
Ralph M. Davenport (son).....	9/22/95
Geraldine Davenport Alsup (granddaughter).....	11/30/22
Glenn Davenport (grandson).....	11/18/29
Homer H. Davenport (son) (no children).....	3/29/02
John R. Davenport (brother).....	2/28/76

It was stipulated that the value of the First Street property on May 23, 1939, was \$40,000.00 and at that time it was rented for a fair gross rental of \$5,400.00 per year. The taxes for 1939 were \$526.52 and the expenses of upkeep were as follows:

1940.....	\$ 8.62
1941.....	_____
1942.....	63.02
1943.....	350.70
1944.....	1,297.78

Levi M. Davenport paid the taxes on the First Street property for the years 1940 to 1944, inclusive, but petitioner paid the above-mentioned upkeep expenses for the years 1940 to 1944, inclusive. [90]

It was stipulated that the value of the First Street property on May 31, 1941, was \$40,000.00 and at that time it was rented for a fair gross rental of \$5,400.00 per year. The taxes for 1941 were \$450.62.

It was stipulated that the value of the Davenport home as of May 31, 1941, was \$15,500.00 and the fair rental value thereof was \$1,500.00 per year. The taxes and other expenses of upkeep of said property were as follows:

Year	Taxes	Other Expenses
1941	\$481.49	\$1,040.65
1942	324.60	1,050.32
1943	296.52	113.62
1944	380.19	519.24

It was further stipulated that the value of properties transferred to petitioner's transferor on June 1, 1939, by Barbara N. Davenport was \$8,500.00 and the fair rental value thereof was \$740.00 per year.

It was further stipulated that Levi M. Davenport turned over to petitioner in the years 1940 to 1944, inclusive, \$432.25 which was part of the money he received from renting rooms in the Davenport home.

It was further stipulated that in 1940 petitioner paid Lucile Weller, daughter of Levi M. Davenport, [91] \$1,000.00 and in 1941 paid Homer Davenport, the son of Levi M. Davenport, \$625.00.

It was further stipulated that the \$1,000.00 paid to Lucile Weller and the \$625.00 paid to Homer Davenport were not deducted in arriving at the taxable net income or book net income in Joint Exhibit 17-Q. Further, that the gross income of the First Street property is not included as gross income in Joint Exhibit 17-Q as Levi M. Davenport collected the gross income from the First Street property from the tenants.

It was stipulated that petitioner made contributions to organizations exempt from income tax under Section 101(6) of the Internal Revenue Code as follows: [92]



1. LaVerne College.....	\$1,500.00	\$3,900.00	\$3,600.00	\$3,656.65	\$3,600.00
2. Los Angeles Tuberculosis & Health Association .....			2.00		
3. Pasadena War Chest.....				50.00	
4. American Red Cross.....				50.00	200.00
5. Children's Home Society of California .....				2.00	
6. Bible Institute of Los Angeles, Inc. (Talbot Radio Program) .....			6.44		35.00
7. Gospel Broadcasting Association (Fuller Radio Program) .....				5.00	45.00
8. Kings Ambassador Evangelistic Association (Chas. Johnson Radio Program) .....				25.00	110.00
9. Union Rescue Mission, Los Angeles, California .....					30.00
10. United China Relief.....				150.00	100.00
11. American Bible Society.....			100.00	175.00	500.00
12. Committee of Mercy, New York City, N. Y.....				50.00	
13. Boys Club of America.....					10.00
14. American Mission to Lepers.....					20.00
15. Gideons International.....					100.00
16. Christian Mission Alliance.....					500.00
17. Church of the Brethren.....			25.00	155.00	25.00
18. Bible Crusaders.....					100.00
19. First Hebrew-Christian Synagogue	1.00		175.00	348.00	500.00
20. Americanism Educational League..			10.00	10.00	10.00
Totals .....	\$1,501.00	\$3,900.00	\$3,918.44	\$4,676.65	\$5,885.00

It was further stipulated that petitioner made contributions to organizations for which no known exemption from income tax has been granted, as follows:

	1940	1941	1942	1943	1944
1. United American Defense Committee .....		\$25.00			
2. National Voice.....			\$15.00	\$15.00	\$ 35.00
3. Phillips China Relief.....					150.00
4. Radio Gospel Hour (Dr. M. H. Fagan) .....				5.00	35.00
5. W. N. Miles Radio Program.....					10.00
6. Flora, Evangelist.....				8.00	
7. State-Wide Committee, Higher Education .....					2.00
8. Los Angeles Times.....			24.50		
9. Democratic Club for Wilkie, Los Angeles .....	14.18				
10. Jeffersonian Democrats, Los Angeles .....	10.00	25.00			
11. Republican Club, Los Angeles, Cal.					25.00
12. Democrat Club, Los Angeles, Cal...					25.00
Totals .....	\$24.18	\$50.00	\$39.50	\$73.00	\$282.00

<sup>1</sup>But see testimony of Fred A. Flora.

<sup>2</sup>But see testimony of J. E. Steinour.

It was further stipulated that the Property Owners Association of California, Los Angeles, California, is exempt from income tax under the provisions of Section 101(8) of the Internal Revenue Code.

There was introduced into evidence the following certificate:

“In the Superior Court of the State of California in and for the County of Los Angeles. No. Pasa P-7290. In the Matter of the Estate of Levi M. Davenport, Deceased.

Certificate

State of California,  
County of Los Angeles—ss.

I, J. F. Moroney, County Clerk and ex-officio Clerk of the Superior Court, within and for the County and State aforesaid, do hereby certify that according to the records on file in my office, Levi M. Davenport died on or about the 6th day of January, 1947, and that said deceased died intestate according to the best knowledge, information and belief of petitioner, Ralph M. Davenport.

I further certify that Ralph M. Davenport is the duly appointed, qualified and acting Administrator of the estate of Levi M. Davenport, Deceased, and that his Letters have not been revoked and are in full force and effect on this date.

In Witness Whereof, I hereunto set my hand and affix the seal of the Superior Court this 24th day of February, 1947.

J. F. MORONEY,  
County Clerk and ex-officio Clerk of the Superior Court of the State of California, in and for the County of Los Angeles.

[Seal] By J. M. GARLAND,  
Deputy." [94]

There was introduced into evidence as petitioner's Exhibit 4 a certificate of the Clerk of the Superior Court of the State of California in and for the County of Los Angeles, as follows:

"In the Superior Court of the State of California in and for the County of Los Angeles. No. Pasa P-7290. In the Matter of the Estate of Levi M. Davenport, Deceased.

#### Certificate

State of California,  
County of Los Angeles—ss.

I, J. F. Moroney, County Clerk and ex-officio Clerk of the Superior Court, within and for the County and State aforesaid, do hereby certify that according to the records on file in my office, Levi M. Davenport died on or about the 6th day of January, 1947, and that said deceased died intestate according to the best knowledge, information and belief of petitioner, Ralph M. Davenport.



I further certify that Ralph M. Davenport is the duly appointed, qualified and acting Administrator of the estate of Levi M. Davenport, Deceased, and that his Letters have not been revoked and are in full force and effect on this date.

In Witness Whereof, I hereunto set my hand and affix the seal of the Superior Court this 24th day of February, 1947.

J. F. MORONEY,  
County Clerk and ex-officio Clerk of the Superior Court of the State of California, in  
and for the County of Los Angeles.

[Seal] By J. M. GARLAND,  
Deputy." [95]

Petitioner, The Davenport Foundation, submits the foregoing as a true and correct statement of all of the evidence material to this appeal which was submitted before the Tax Court of the United States and prays that the same may be approved and filed as a part of the record in this cause.

/s/ MELVIN D. WILSON,  
Attorney for Petitioner.

Service is acknowledged this 19th day of April, 1948, and agreed to.

/s/ CHARLES OLIPHANT, AWS  
Chief Counsel, Bureau of  
Internal Revenue. [96]

## JOINT EXHIBIT 1-A

## Declaration of Trust No. 1

Know All Men by These Presents:

This Agreement made and entered into this 23rd day of May, 1939, by and between Levi M. Davenport of 674 Elliot Drive, Pasadena, California, hereinafter referred to as Trustor, and La Verne College, a corporation, incorporated under Title XVII Part 4, Division 1 (Sections 649 to 651) Civil Code of the State of California, hereinafter referred to as Trustee, and C. Ernest Davis, Lucile Davenport Weller, J. E. Steinour, Fred A. Flora and L. E. Miller, constituting a Board of Directors, hereinafter referred to as the Board.

Witnesseth: That

Whereas, the Trustor is desirous of establishing a permanent foundation to be known as "The Davenport Foundation" for the purposes hereinafter provided.

Now Therefore, the Trustee hereby declares that the Trustor has transferred and delivered to it without consideration moving from the Trustee all his right, title and interest in and to the property described in Schedule "A" hereto attached and by this reference made a part hereof. [97]

All property now, or hereafter, subject to this Trust shall constitute the "Trust Estate."

The only duty, or obligation of the Trustee shall be to hold Title to the Trust Estate in Trust, subject to the management, control and direction of the Board. It's duties shall be entirely Ministerial, that

## Joint Exhibit 1-A—(Continued)

is to say, it shall perform such acts as shall be necessary to carry out the orders and directions of the Board.

The Board shall act as and constitute the Board of Trustees of the Foundation and shall have complete control, management, and operation of the property forming the Trust Estate, and shall receive and collect the principal and the income of the Trust Estate, and after the payments and deductions hereinafter mentioned, shall pay and/or accumulate, and/or use and invest, hold, apply and distribute the same to, or for the purposes hereinafter stated, and shall cause the Trustee to convey and transfer the corpus or principal, or portions of the Trust Estate, together with accumulations, if any, as hereinafter provided.

## Reserves

Before distribution is made of any of the net income reserves shall be set aside as follows to-wit:

- (1) 25% of the gross income for taxes, supervision and upkeep. [98]
- (2) 12% of the gross income for replacements and betterments.

## Distribution of Income

All the net income available for distribution shall be paid in monthly installments, as follows:

- (1) To the Trustor, Levi M. Davenport, the sum of Four Hundred Dollars (\$400.00) per month, for and during the term of his natural life.

## Joint Exhibit 1-A—(Continued)

- (2) To LaVerne College, a corporation, the sum of Three Hundred Dollars (\$300.00) per month for the purpose of establishing a department of Philosophy and Religion, which department shall be established at the beginning of the school year 1939-1940.
- (3) To make suitable and proper provision for the support and maintenance of J. R. Davenport, my brother, as his needs may require, not to exceed however, One Hundred Dollars (\$100.00) per month, all of which shall be at the sole discretion of the Board of Trustees. In the event that any of my children should come to want, the Board of Trustees shall use a portion of the income to care for them in so far as their needs may require, all of which shall also be solely within the discretion of the Board of Trustees.
- (4) To American Bible Society, with its principal office at Bible House, New York City, the sum of Three Hundred Dollars (\$300.00), per annum, payable annually at the discretion of the Board.
- (5) To the payment of annuities in such amounts as may be agreed upon between the Board of Trustees and the annuitants, who may add to this Trust.
- (6) All of the rest and residue of undistributed income shall be used by the Board of Trustees for such purposes consistent with the



## Joint Exhibit 1-A—(Continued)

purposes of this trust as may be determined in the sole discretion of said Board of Trustees.

The courses to be given and taught by said department of Philosophy and Religion, shall be along the general line of the following suggested program:

**Orientation**

Chapel lectures and services designed to help the student adjust himself in a Christian manner to life in the school and in the world. [100]

**History of**

The Church,

The Church of the Brethren,

Religion,

Religious Education, all of which shall be taught from the Christian point of view.

**Bible**

Sound courses in the Word of God shall be the basis of the work in the whole department and should be regarded as a basic part of one's education at LaVerne College.

**Philosophy**

Strong courses that will give the student an evangelical, theistic point of view and unify his ideas into a harmonious Christian faith. Such courses as Ethics, the Psychology of religion, Philosophy of Religion, and the Philosophy of the Christian Religion will be included.

## Joint Exhibit 1-A—(Continued)

## Religious Education

Courses that will help one to become an intelligent, capable worker in the Church's great program of Christian instruction.

## Sociology

Religion applied to life, to help the student to think through the practical application of the principles and teachings of the word of God as exemplified in Scriptures to the problem of our modern world, one particular addition that we desire to be made to our present offerings in this field is a good course of Rural Sociology. We need this because we have so many country churches in our brotherhood. The country is suffering throughout America today. Something needs to be done for rural life and it is a problem in which even our State and National governments are interested.

## A Practical Work Program

To give opportunity for selected students to serve as Sunday School teachers, club leaders for boys and girls, mission workers etc., in a program of church work and home missions, this program to be developed perhaps in cooperation with our District Mission Board or other agencies. All teaching shall be in harmony with the philosophy of creation, according to the account in the Book of Genesis, Chapters 1 and 2. [101]

## Vacancies on Board of Trustees

It is my desire that one of my children, and after they have passed on to their reward, one of my

## Joint Exhibit 1-A—(Continued)

grandchildren, shall serve on the Board of Trustees, and any vacancy on said Board caused by the death of my daughter, Lucile, or any of my children, or grandchildren, shall be filled by the Board from among my surviving children and grandchildren. The Elders body of the Church of the Brethren of the District of Southern California and Arizona shall pass upon and determine the qualifications and fitness of any of my children or grandchildren, for service on said Board of Trustees, and none of my children or grandchildren shall serve upon said Board unless said Elders body shall determine that he or she is a fit and qualified person for such service. After the death of all of my children and grandchildren, such vacancies shall be filled in the same manner as provided herein for the election of the other members of the Board, and the person appointed as herein provided shall be a member of the Church of the Brethren.

All other vacancies on said Board shall be filled by nominations made by the Board of Trustees and submitted to the Elders Body of the Church of the Brethren of the District of Southern California and Arizona, from which nominations the Elders body shall fill said vacancies unless [102] said body should determine that none of the nominees are qualified, in which event the Board of Trustees shall make further and additional nominations, from which the Elders body may fill such vacancies. All the persons elected by the Elders Body as afore-

## Joint Exhibit 1-A—(Continued)

said to said Board of Trustees, or appointed as herein provided, shall be persons who can by their life and conduct subscribe to the following:

1. The Divine Authority and the full and complete inspiration of the whole of the Old and New Testament Scriptures.
2. The Deity of our Lord Jesus Christ.
3. The Doctrine of the Trinity.
4. The Fall of Man and his consequent depravity and the necessity of the New Birth.
5. The sinless life of Jesus Christ, Atonement in His blood which was shed for sin, and His personal Resurrection.
6. Justification by faith in our Lord Jesus Christ.
7. Regeneration by the Word and the agency of the Holy Spirit.
8. The personality of the Holy Spirit and as the Divine Paraclete, the Comforter and [103] the Guide of the people of God.
9. Sanctification through the Word and Spirit.
10. The Personal and Visible Return of our Lord Jesus Christ, the Resurrection of the Dead, and the last judgment.
11. That the Scriptures of the Old and New Testaments are inspired of God, and are inerrant in the original writings, and that they are the supreme and final authority in faith and life, and who believe in one God, eternally existing in three persons, Father, Son, and Holy Spirit; that Jesus was begotten by the



## Joint Exhibit 1-A—(Continued)

Holy Spirit, and born of the Virgin Mary, and is true God and true Man, that man was created in the image of God, that he sinned and thereby incurred not only physical death, but also that spiritual death which is separation from God; that the Lord Jesus Christ atoned for our sins according to the Scriptures, and all that believe on him, and are Baptised by Water and of the Spirit are justified by the blood that He shed on the Cross of Calvary; that Jesus was crucified, rose from the dead, and is now seated at the [104] right hand of the Father interceeding for us as your High priest and advocate; who believe in the personal and imminent return of our Lord and Saviour Jesus Christ according to the Scriptures; and believe in the bodily resurrection of the just and the unjust.

## Removal From the Board of Trustees

Should any of the members of the Board of Trustees for any cause or reason become unfit to serve on the Board or become ethically, or scripturely embroiled in the evil things of this world, the remaining members of the Board may file a complaint with the Elders Body of the Church of the Brethren of the District of Southern California and Arizona. A time and place for hearing the complaint shall be set and the decision of said Elders bodies shall be final. The procedure in matters of removal shall be established by the Elders body.

## Joint Exhibit 1-A—(Continued)

## Reservations

It is understood and agreed that during the lifetime of the Trustor, Levi M. Davenport, that the Trustor [105] shall have the right to the use and occupation, rent free, of the home now occupied by him at 674 Elliot Drive, Pasadena, California, or some other home of similar rental value.

## Compensation of Trustee

The members of the Board of Trustees shall be paid for their services at the same rate as is paid at the time for comparable services and actual expenses incurred. The amount shall be fixed by the Board.

We hope and pray that all those having to do with the management of this Foundation will have the sacrificial Spirit. Thus the work will grow and prosper, God will be glorified and our Lord will be lifted up before a dying world.

## Additions to the Foundation

Others may add to this Foundation, provided the additional income shall be used in maintaining the Doctrines and Principles of our church, as herein set forth, provided however, that the donor may reserve a portion of such income for himself or herself, or for relatives during his, her, or their lifetime. [106]

## Change of Beneficiary

Should LaVerne College fail to establish such department of Philosophy and Religion, and to carry

## Joint Exhibit 1-A—(Continued)

out the teachings as herein enunciated, or should it be merged into or consolidated with any other Educational or Charitable Institution, or cease to exist as an institution of learning, the Trustees shall pay the income herein provided to be paid to it, to some other institution, or institutions, within our denomination as determined by said Board, and in such event the Board of Trustees shall designate some other Trustee, or Trustees to hold title to the Trust Estate and LaVerne College, or its last Board of Trustees, shall convey the title of the Trust Estate to such new Trustee so designated by said Board.

## Powers of Trustees

To carry out the express purposes of this trust and in aid of its execution and the proper administration, management and disposition of the trust estate, the Board of Trustees is vested with the following additional powers and discretions.

At its option and as long as it may deem advisable, to retain any property which it may receive hereunder. [107] To manage, control, sell, convey, partition, divide, subdivide, exchange, improve, repair and to encumber by mortgage, trust deed or otherwise and in such manner and in accordance with such procedure as it may deem advisable, the trust estate or any part thereof. To lease the trust estate, or any part thereof, and to grant the right to mine or drill for and remove therefrom gas, oil, and/or any other minerals. To invest the principal (and income if accumulated) in any property,

## Joint Exhibit 1-A—(Continued)

whether or not permissible by law as investment for trust funds. To determine, in its discretion, what is principal of the trust estate, gross income, or net distributable income therefrom; except that all bonuses, royalties and recoveries from mines, gas or oil leases and/or wells, all stock dividends and stock rights, and all gain or loss realized on payment, retirement or sale of stocks, notes, bonds or other securities shall inure to or fall upon principal, and all cash dividends (other than liquidating dividends stated in writing to be such by the corporation paying the same) shall go to income of the trust estate. To have respecting bonds, shares of stock and other securities, all the rights, powers and privileges of an owner, including, though without limiting the foregoing, voting, giving proxies, payment of calls, assessments and other sums deemed by the Board expedient [108] for the protection of the interests of the trust estate, exchanging securities, selling or exercising stock subscription or conversion rights, participating in foreclosures, reorganizations, consolidations, mergers, liquidations, pooling agreements, voting trusts, assenting to corporate sales, leases and encumbrances. All discretions in this trust conferred upon the Board of Trustees shall, unless specifically limited, be absolute and uncontrolled and their exercise conclusive on all persons interested in this trust or the trust estate. The powers and discretions of the Board enumerated herein are not to be construed as a limitation upon its general powers and discretions but



## Joint Exhibit 1-A—(Continued)

the Board of Trustees in addition thereto is hereby vested with and shall have, for the full duration of this trust, as to the trust estate, the income therefrom, and in the execution of this trust, the same and all the powers and discretions that an absolute owner of property has or may have. The right to encumber the trust estate shall be limited to 10% of the gross value thereof.

The whole title, legal and equitable, in fee, to the trust estate is and shall be vested in the Trustee as such title in the Trustee is necessary for the due execution of this trust by the Board of Trustees as herein provided. The beneficiaries, except as herein provided take no estate or interest therein and their interests [109] hereunder are personal property only, consisting of the right to enforce the due performance of this trust.

Each beneficiary hereunder is hereby restrained from anticipating, encumbering, alienating or in any other manner assigning his or her, or its interest or estate in either principal or income, and is without power so to do, nor shall such interest or estate be subject to any beneficiary's obligations or liabilities, nor to judgment or other legal process, bankruptcy proceedings or claims or creditors or others.

The Board of Trustees in its sole discretion may advise or consult with the Trustor regarding the sale or retention of properties belonging to the trust estate and the investment of sums of money constituting a part thereof, or the exercise of any of

## Joint Exhibit 1-A—(Continued)

its other powers or discretions as such Board of Trustees has hereunder, and in following in whole or in part any requests, recommendations or approvals of such Trustor, the Board of Trustees shall be free from responsibility for any losses or liabilities which may result to the trust estate, the Board of Trustees, and/or any beneficiary hereunder by reason thereof. Such request, recommendation or approval shall be deemed to be duly authorized by the Trustor if contained in written instrument executed on behalf of the Trustor.

After the death of the Trustor and the individual beneficiaries herein named, the Board of Trustees is hereby authorized to incorporate the Foundation if in its sole discretion it seems best and advantageous so to do, and in such event LaVerne College shall convey all of its title in the Trust Estate to such corporation upon request of the Board.

In the event that any provision or provisions of this instrument are or are adjudged to be for any reason unenforceable the remainder hereof, disregarding such provisions, shall subsist and be carried into effect.

This trust may not be revoked nor, except as otherwise herein provided may any of the corpus of the trust estate be withdrawn.

Executed in triplicate.

In Witness Whereof the Trustor has hereunto set his hands and seal, and LaVerne College as Trustee has caused these presents to be subscribed by its

Joint Exhibit 1-A—(Continued)

President and Secretary thereunto duly authorized  
this 23rd day of May, 1939.

LEVI M. DAVENPORT,  
Trustor.

[Corporate Seal]

LA VERNE COLLEGE,  
By EDGAR ROTHROCK,  
President,  
By J. D. BRANDT,  
Secretary. [111]

The undersigned Trustor does hereby certify that said Declaration of Trust fully and correctly sets out the terms and trusts under which the Trust Estate is to be held, managed and disposed of by the Board of Trustees therein named, and does hereby consent to approve, ratify and confirm the same in all particulars.

LEVI M. DAVENPORT,  
Trustor.

I, Barbara N. Davenport, wife of the Trustor, Levi M. Davenport, do hereby certify that I have read the above Declaration of Trust and I hereby agree, consent to, approve and ratify the same in all particulars.

BARBARA N. DAVENPORT.

The undersigned designated as the Board of Trustees to manage, control and operate the Foundation and the Trust Estate, do hereby each agree to act as a member of said Board and to be bound

by the terms and provisions of the said Declaration of Trust.

C. ERNEST DAVIS,  
LUCILE DAVENPORT  
WELLER,  
FRED A. FLORA,  
J. E. STEINOUR,  
L. E. MILLER. [112]

BY-LAWS OF  
THE DAVENPORT FOUNDATION

By-Laws and Regulations, Except as Otherwise Provided by Statute or the Declaration of Trust Under Which the Same was Established.

Article I.

Section 1. Principal Office. The principal office for the transaction of business of the Foundation is hereby fixed at ..... in the City of Pasadena, County of Los Angeles, State of California.

The Board of Trustees shall have power and authority to change said principal office from one location to another, and the Secretary shall note any such change opposite this Section.

Article II.

Section 1. Trustees. Subject to such limitations as may be prescribed by law all of the powers of the Foundation shall be exercised by, [113] or under the authority of and the business and the affairs of the Foundation shall be controlled by the Board of Trustees. Without prejudice to such general powers, but subject to the same limitations, it is



hereby expressly declared that the Board of Trustees shall have the following powers:

First: To select and remove all the other officers, agents and employees of the Foundation, prescribe such powers and duties for them as may not be inconsistent with law, the Declaration of Trust or the By-Laws, fix their compensation and require from them security for faithful service.

Second: To conduct, manage and control the affairs and business of the Foundation, and to make such rules and regulations therefor not inconsistent with law, the Declaration of Trust, or the By-Laws, as they may deem best.

Third: To borrow money and incur indebtedness and to cause to be issued therefor in the name of the Foundation, promissory notes, deeds of Trust, mortgages, pledges, [114] hypothecations, or other evidence of debt, and securities therefor. Subject to the limitations contained in the Declaration of Trust.

Fourth: To appoint an Executive Committee and other committees and to delegate to the executive committee any of the powers and authority of the Board in the management of the business and affairs of the Foundation. The Executive Committee shall be composed of two or more members of the Board of Trustees.

Section 2. Number and Qualification of Trustees. The authorized number of Trustees shall be five (5), and their qualifications shall be as set forth in the Declaration of Trust.

Section 3. Election and Term of Office. The

members of the first Board of Trustees shall hold office until their successors are elected and qualified. They shall be elected, and vacancies shall be filled as provided in the Declaration of Trust.

Section 4. Place of Meeting. Regular meetings of the Board of Trustees shall be held at Pasadena, California, or at such other place as the Board of Trustees shall designate by Resolution or by written consent of all members of the Board.

Section 5. Organization Meeting. Immediately following the execution of the Declaration of Trust by [115] the members of the Board of Trustees, and annually thereafter, the Board shall hold a regular meeting for the purpose of organization, election of officers and the transaction of the business. Notice of such meeting is hereby dispensed with.

Section 6. Regular Meetings. The regular annual meeting of the Board of Trustees shall be held on the third day of January at 9:30 o'clock A.M. of said day of each year, provided however, should said day fall upon a legal holiday then said meeting shall be held at the same time on the next day thereafter ensuing which is not a legal holiday.

Other Regular Meetings. Other regular meetings of the Board shall be held within call on the first Tuesday of April, July and October of each year, at 9:30 o'clock A.M. of said day; provided, however, should said day fall upon a legal holiday, then said meeting shall be held at the same time on the next day thereafter ensuing, which is not a legal holiday. Notice of all such regular meetings of the Board of Trustees is hereby dispensed with.

Section 7. Special Meetings. Special meetings of the Board of Trustees for any purpose or purposes shall be called at any time by the President or if he be absent or unable, or refuses to act by any Vice-President or by two Directors. [116]

Written notice of the time and place of special meetings shall be delivered personally to the Trustees or sent to each Trustee by mail or other form of written communication, charges prepaid, addressed to him at his address as it is shown upon the Records of the Foundation, or if it is not so shown on such records or is not readily ascertainable, at the place in which the meetings of the Trustees are regularly held. In case such notice is mailed, or telegraphed, it shall be deposited in the United States Mail, in any place in the County of Los Angeles, or delivered to any Telegraph Company in any place in Los Angeles County, California, at least three days prior to the time of the holding of the meeting. In case such notice is delivered as above provided; it shall be so delivered at least three days prior to the time of the holding of the meeting. Such mailing, telegraphing or delivery as above provided shall be due, legal and personal notice to such Trustee. [117]

Section 8. Notice of Adjournment. Notice of the time and place of holding an adjourned meeting need not be given to absent Trustees if the time and place be fixed at the meeting adjourned.

Section 9. Entry of Notice. Whenever any Trustee has been absent from any special meeting of the Board of Trustees, an entry in the minutes to the effect that notice has been duly given shall be

conclusive and incontrovertible evidence that due notice of such special meeting was given to such Trustee, as required by law and the By-laws of the Foundation.

Section 10. Waiver of Notice. The transactions of any meeting of the Board of Trustees, however called and noticed or wherever held, shall be as valid as though had at a meeting duly held after regular call and notice, if a quorum be present, and if, either before or after the meeting, each of the Trustees not present sign a written waiver of notice or a consent to holding such meeting or an approval of the minutes thereof. All such waivers, consents or approvals shall be [118] filed with the records or made a part of the minutes of the meeting.

Section 11. Quorum. A majority of the authorized number of Trustees shall be necessary to constitute a quorum for the transaction of business, except to adjourn as hereinafter provided. Every act or decision done or made by a majority of the Trustees present at a meeting duly held at which a quorum is present shall be regarded as the act of the Board of Trustees, unless a greater number be required by law.

Section 12. Adjournment. A quorum of the Trustees may adjourn any Trustees' meeting to meet again at a stated day and hour; provided, however, that in the absence of a quorum, a majority of the Trustees present at any Trustees' meeting, either regular or special, may adjourn from time to time until the time fixed for the next regular meeting of the Board.



Section 13. Fees and Compensation. Trustees shall not receive any stated salary for their services as Trustees, but, by resolution of the Board, a fixed fee, with or without expenses [119] of attendance, may be allowed for attendance at each meeting. Nothing herein contained shall be construed to preclude any Trustee from serving the Foundation in any other capacity as an officer, agent, employee, or otherwise, and receiving compensation therefor. All of which shall be subject, however, to the terms and provisions of the Declaration of Trust.

### Article III.

Section 1. Officers. The officers of the Foundation shall be a President, a Vice-President, a Secretary, and a Treasurer. The Foundation may also have, at the discretion of the Trustees, a chairman of the Board, one or more additional Vice-Presidents, one or more assistant secretaries, one or more assistant treasurers, and such other officers as may be appointed in accordance with the provisions of Section 3 of this Article. All officers must be Trustees. One person may hold two or more offices, except those of President and Secretary.

Section 2. Election. The officers of the Foundation, except such officers as may be [120] appointed in accordance with the provisions of Section 3 or Section 5 of this Article, shall be chosen annually by the board of trustees, and each shall hold his office until he shall resign or shall be removed or otherwise disqualified to serve, or his successor shall be elected and qualified.

Section 3. Subordinate Officers, etc. The Board

of Trustees may appoint such other officers as the business of the Foundation may require, each of whom shall hold office for such period, have such authority and perform such duties as are provided in the By-laws or as the Board of Trustees may from time to time determine.

Section 4. Removal and Resignation. Any officer may be removed, either with or without cause, by a majority of the Trustees at the time in office, at any regular or special meeting of the Trustees, or except in case of an officer chosen by the Board of Trustees, by any officer upon whom such power of removal may be conferred by the Board of Trustees.

Any officer may resign at any time by giving written notice to the Board of Trustees or to the President, or to the Secretary of the Foundation. Any such resignation shall take effect at the date of the receipt of such notice or at any later time specified therein; and, unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

Section 5. Vacancies. A vacancy in any office because of death, resignation, removal, disqualification or any other cause, shall be filled in the manner prescribed in the By-laws for regular appointments to such office.

Section 6. Chairman of the Board. The chairman of the Board, if there shall be such an officer, shall, if present, preside at all meetings of the Board of Trustees, or prescribed by the By-laws.

Section 7. President. Subject to such super-

visory powers, if any, as may be given by the Board of Trustees to the chairman of the [122] Board, if there be such an officer, the president shall be the chief executive officer of the Foundation and shall, subject to the control of the Board of Trustees, have general supervision, direction and control of the business and officers of the Foundation. He shall preside at all meetings of the Trustees in the absence of the chairman of the Board. He shall be ex-officio a member of all the standing committees including the executive committee, if any, and shall have the general powers and duties of management usually vested in the office of president of a Foundation, and shall have such other powers and duties, as may be prescribed by the Board of Trustees or the By-laws.

Section 8. Vice-President. In the absence or disability of the president, the vice-presidents in order of their rank as fixed by the Board of Trustees, or if not ranked, the vice-president designated by the Board of Trustees, shall perform all the duties of the President, and when so acting shall have all the powers of, and be subject to [123] all the restrictions upon, the president. The vice-presidents shall have such other powers and perform such other duties as from time to time may be prescribed for them respectively by the Board of Trustees or the By-laws.

Section 9. Secretary. The secretary shall keep, or cause to be kept, a book of minutes at the principal office or such other place as the Board of Trustees may order, of all meetings of trustees, with the

time and place of holding, whether regular or special and if special, how authorized, the notice thereof given, the names of those present at trustees' meetings, and the proceedings thereof.

The Secretary shall give, or cause to be given, notice of all the meetings of the Board of Trustees required by the By-laws or by law to be given, and shall have such other powers and perform such other duties as may be prescribed by the Board of Trustees or the By-laws. [124]

Section 10. Treasurer. The treasurer shall keep and maintain, or cause to be kept and maintained, adequate and correct accounts of the properties and business transactions of the Foundation, including accounts of its assets, liabilities, receipts, disbursements, gains, losses, capital, and surplus. The books of account shall at all times be open to inspection by any Trustee.

The treasurer shall deposit all moneys and other valuables in the name and to the credit of the Foundation with such depositaries as may be designated by the Board of Trustees. He shall disburse the funds of the Foundation as may be ordered by the Board of Trustees, shall render to the president and Trustees, whenever they request it, an account of all of his transactions as treasurer and of the financial condition of the corporation, and shall have such other powers and perform such other duties as may be prescribed by the Board of Trustees or the By-laws. [125]



## Article IV.

### Miscellaneous

Section 1. Checks, Drafts, etc. All checks, drafts or other orders for payment of money, notes or other evidences of indebtedness, issued in the name of or payable to the Foundation, shall be signed or endorsed by such person or persons and in such manner as, from time to time, shall be determined by resolution of the Trustees.

Section 2. Annual Report. The Board of Trustees of the Foundation shall cause to be sent to the District Conference of the Church of the Brethren of the Southern District of California and Arizona not later than twenty days before the Annual Meeting of said District Conference, an annual report of the business of the Foundation.

Section 3. Contract, etc., How Executed. The Board of Trustees, except as in the By-laws otherwise provided, may authorize any officer or officers, agent or agents, to enter into any contract or execute any instrument in the name of and on behalf of the Foundation, and such authority may [126] be general or confined to specific instances; and unless so authorized by the Board of Trustees, no officer, agent or employee shall have any power or authority to bind the Foundation by any contract or engagement or to pledge its credit or to render it liable for any purpose or to any amount.

## Article V.

### Amendments

Section 1. Power of Trustees. New By-laws may be adopted or these By-laws may be amended or repealed by the Board of Trustees. [127]

## Certificate of Secretary

I, the undersigned, do hereby certify:

(1) That I am the duly elected and acting secretary of The Davenport Foundation; and

(2) That the foregoing By-laws, comprising Fifteen (15) pages constitute the original By-laws of said Foundation as duly adopted at the first meeting of the Board of Trustees thereof duly held Tuesday, May 23, 1939.

In Witness Whereof, I have hereunto subscribed my name this 23rd day of May, 1939.

FRED A. FLORA,

Secretary [128]

## JOINT EXHIBIT 4-D

TRANSFER AND ACCEPTANCE OF  
ADDITIONAL PROPERTY UNDER TRUST

## Addition No. 1 to Trust No. 1

To La Verne College, a Corporation, Trustee Under  
Declaration of Trust No. 1

Pasadena, California

June 1, 1939.

Whereas, on or about the 23rd day of May, 1939, Levi M. Davenport, husband of the Trustor herein, conveyed and transferred to LaVerne College as Trustee, certain property described in a Declaration of Trust executed by LaVerne College as Trustee, which declaration of Trust reserved unto the Trustor and others, the right to add other property to the Trust Estate thereunder.

Now, Therefore, I, Barbara N. Davenport, wife of said Trustor, do hereby deliver to you herewith, property and instruments of transfer listed below. Such right, title and property as is received by you by virtue of such delivery shall from the date of its acceptance by you become a part of said Trust Estate, subject to all the terms of said trust, except as follows:

(1) I hereby reserve the right to collect and retain for my own use, all of the income of the property [129] hereby transferred for and during the term of my natural life, and the right to designate for a period of time which shall not exceed the life, or lives of persons in being, the use to which one-half of the net income may be put after my death. The property hereby conveyed is described as follows:

Parcel 1. Lot 4 of Block "F" of Subdivision No. 1 of Wellington Heights, in the County of Los Angeles, State of California, as per map recorded in Book 5, Page 7 of Maps in the office of the County Recorder of said County, free and clear of all incumbrances, excepting taxes for the fiscal year 1939-40 and conditions, restrictions reservations of record.

Parcel 2. The Northeast Quarter of the Southwest Quarter of Section 19, Township 15, S. Range 19 East M.D.B. & M., in the County of Fresno, State of California.

Pasadena, California.

June 1, 1939.

BARBARA N. DAVENPORT,  
Trustor.

LaVerne, California

June 3, 1939.

The undersigned hereby acknowledge delivery to it of the foregoing, and of the property and instruments above enumerated, which property and all rights, title, and interest received by virtue of such delivery are to be added to and become a part of the Trust Estate [130] under said Declaration of Trust hereinabove referred to, subject to all the terms and conditions thereof, and to the reservations herein contained.

[Seal]

LA VERNE COLLEGE,

As Trustee,

By EDGAR ROTHROCK,

President,

By J. C. BRANDT,

Secretary. [131]

## JOINT EXHIBIT 5-E

## GRANT DEED CORPORATION

Recorded Sept. 18, 1939, 2:29 p.m., Book 16840, Page 258 of Official Records, Los Angeles County, California.

La Verne College, a corporation, in consideration of less than \$100.00 Dollars, to it in hand paid, the receipt of which is hereby acknowledge, does hereby Grant to L. M. Davenport, a married man, whose wife's name is Barbara N. Davenport, all that property in the City of Los Angeles, County of Los Angeles, State of California, described as:

\*

\*

\*

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\*

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\*



In Witness Whereof, the above mentioned corporation has caused this deed to be duly executed and its corporate name to be subscribed hereto by its President and attested by its Secretary, who has hereunto affixed its corporate seal, this 2nd day of September, 1939.

(Corporate Seal)

LA VERNE COLLEGE,  
By EDGAR ROTHROCK,  
President.

Attest:

J. C. BRANDT,  
Secretary. [132]

\* \* \* \* \*

At a special meeting of the Executive Committee of the Board of Trustees of LaVerne College, a corporation, held September 1, 1939, at the Church of the Brethren, in LaVerne, California, the following resolution was adopted:

That, whereas LaVerne College, a corporation, now holds the deed to a property described as follows, to wit:

\* \* \* \* \*

And that whereas LeVerne College, a corporation, holds this property in trust subject to the will of the Board of Trustees of the foundation known as the Davenport Foundation, and that whereas said Board of the Davenport Foundation has asked that the above property be deeded to L. M. Davenport.

Now, Therefore, be it resolved that LaVerne College deed said property to L. M. Davenport, and

Be it further resolved that Edgar Rothrock, President of the Board of Trustees of LaVerne College, a corporation, and J. C. Brandt, Secretary of the same board, be authorized to execute the necessary papers to consummate the transaction.

I, J. C. Brandt, the Secretary of the Executive Committee of the Board of Trustees of LaVerne College, a corporation, certify that the above is a true and correct copy of a resolution passed by said committee, September 1, 1939.

J. C. BRANDT. [133]

#### JOINT EXHIBIT 6-F

On motion by Mr. Steinour, seconded by Mrs. Weller, and carried, the following Resolution was adopted:

Whereas, the title to the property hereinafter described is vested in LaVerne College, a corporation, and

Whereas, it is deemed by this Board for the best interest of the Davenport Foundation that a building be constructed thereon, and that for the purpose that the sum of \$15,000.00 be borrowed therefor and a trust deed given to secure the payment thereof, and

Whereas, La Verne College cannot use its credit for that purpose,

Now, Therefore, Be It Resolved that LaVerne College be and it is hereby requested and in-

structed to convey said property to L. M. Davenport, for the purpose of permitting said L. M. Davenport to borrow thereon funds to construct said building.

The property hereinabove referred to is located in the City of Los Angeles, County of Los Angeles, State of California, and is more particularly described as follows: [134]

\* \* \* \* \*

JOINT EXHIBIT 7-G

GRANT DEED CORPORATION

Recorded Nov. 9, 1940, 10:52 a.m. Book 17928, Page 244 of Official Records, Los Angeles County, California.

La Verne College, a corporation, a corporation, in consideration of less than One Hundred Dollars, to it in hand paid, the receipt of which is hereby acknowledged, does hereby Grant to Levi M. Davenport, a married man, as his separate property, whose wife's name is Barbara N. Davenport, all that property in the City of Pasadena, County of Los Angeles, State of California, described as:

\* \* \* \* \*

In Witness Whereof, the above mentioned corporation has caused this deed to be duly executed and its corporate name to be subscribed hereto by its President and attested by its Secretary, who has

hereunto affixed its corporate seal, this 26th day of March, 1940.

(Corporate Seal)

LA VERNE COLLEGE,  
a Corporation,  
By EDGAR ROTHROCK,  
President.

Attest:

J. C. BRANDT,  
Secretary.  
BARBARA N. DAVENPORT.

\* \* \* \* \*

## JOINT EXHIBIT 8-H

### ARTICLES OF INCORPORATION FOR NON-PROFIT CORPORATION

Know All Men by These Presents: That we, the undersigned, have this day voluntarily associated ourselves together for the purpose of forming a corporation under Title XII, Article I of the "General Nonprofit Corporation Law" of the State of California,

And we hereby certify:

#### Article I.

That the name of the corporation shall be The Davenport Foundation.

#### Article II.

That the purpose for which this corporation is formed are as follows:

1. To act as Trustee under Christian Educational, Charitable, Eleemosynary, and other charitable



## Joint Exhibit 8-H—(Continued)

trusts, receiving, holding, managing, administering and expending property and funds in accordance with the respective trusts upon which the same are acquired and held.

2. To receive and accept all kinds of property by gift, devise, and bequest, subject to such conditions and limitations as may be imposed by the donor, and in connection with property so acquired.

3. To lease, manage, operate, hold, have, use, take possession of and enjoy the same for the uses and purposes of the corporation, and to sell, lease, deed in trust, alien or dispose of the same at the pleasure of the corporation, [136] subject to the terms and conditions under which the same may have been acquired, and for the uses and purposes for which said corporation is formed, and to buy and sell real or personal property necessary and convenient to carry out the purposes of the corporation to borrow money, construct buildings on such real property, and to apply the proceeds of sale, including all and any income, to the uses and purposes of the corporation.

4. In administering any property given, transferred, devised, or bequeathed to the corporation, unless otherwise specifically provided in the particular instrument transferring the particular property to the corporation, the corporation shall be and it is hereby specifically and generally authorized and empowered:

(a) To sell, lease, mortgage, transfer or exchange all or any part of such property at such prices and

## Joint Exhibit 8-H—(Continued)

upon such terms and conditions and in such manner as it may deem best;

(b) To execute and deliver any proxies, powers of attorney or to make, execute and deliver any contracts, deeds and all agreements and other instruments that it may be necessary or proper in the administration of the property.

(c) To invest, reinvest, loan and re-loan the whole or any portion of the trust estate conveyed to it in such, any, and all ways, properties or securities, and upon such terms and conditions as it may deem best, without restrictions to the character or class of loans and investments permitted to trust estates or trust companies. [137]

(d) To determine whether money or property coming into its possession shall be treated as principal or income, and charge or apportion any expenses or losses to principal or income as it may deem best or equitable;

(e) To select and employ in and about the execution of its business, all employees, agents, and attorneys it may deem necessary, and to pay the reasonable compensation and expenses;

(f) To do all and any other acts and things not hereinbefore specified which it may deem advisable, or which changed or varying conditions, laws, or circumstances may render necessary, or advisable to the end that the purposes of the corporation may be carried out.

(g) To have as to the trust estate and in the execution of its trusts, all the powers and discre-

## Joint Exhibit 8-H—(Continued)

tions now or hereafter given to and conferred upon Trustees by law and in addition thereto all other powers and discretions that an absolute owner of property has or may have, but subject at all times to accountability for the prudent exercise thereof; in particular to have, respective bonds, shares of stock, and other securities received by it under any trust or trusts, the power of voting, giving proxies, payment of calls, assessments, and other sums necessary or expedient for the protection of the interests of the trust, participating and voting trusts, pooling agreements, assenting to corporate sales and other corporate acts, selling or exercising stock subscriptions, conversions, rights, participating in foreclosures, reorganizations, consolidations, [138] mergers, and liquidations; and in connection with any such proceedings to deposit securities with and transfer title to any protective or other committee representing the holders of such securities, or some portion thereof.

(h) To enter into any and all settlements, adjustments, or compromises deemed by the corporation necessary or expedient in order to settle and to institute or defend all suits, or other proceedings necessary to determine contests, or controversies, under wills, trust agreements or other instruments or in any manner arising related to or affecting property, devised or bequeathed or otherwise transferred to the corporation or the rights or claims of the corporation under such instruments; for such consideration as the corporation may deem adequate

## Joint Exhibit 8-H—(Continued)

to convey and transfer prior or subsequent to distribution to or acceptance thereof by the corporation, rights and interests, present or future, which may pass to the corporation under wills or other instruments; and in general to do any and all things deemed by the corporation necessary to protect its interests in respect to property rights or interests, devised or bequeathed or otherwise transferred to it.

(i) To do each and every thing necessary, appropriate or adapted to carry into effect any and all of the foregoing purposes and powers, or to attain the objects of the corporation herein enumerated, or which at any time appears conducive to or expedient for the benefit and protection of the corporation, and generally to do any act or transact any business in connection with the said purposes, [139] powers which a copartner or a natural partner could do or exercise and which now or hereafter may be authorized by law, and to do each and every thing necessary in connection with the foregoing or calculated directly or indirectly to promote the interests of the corporation, and to protect and preserve the property held by it in accordance with and pursuant to the terms and conditions under which the property may have been received by the corporation.

This corporation is one which does not contemplate pecuniary gain or profit to the members thereof.

## Article III.

That the existence of this corporation is to be perpetual.



## Joint Exhibit 8-H—(Continued)

## Article IV.

That the County in the State of California where the principal office for the transaction of the business of this corporation is to be located is Los Angeles County.

## Article V.

That the names and addresses of the persons who are to act in the capacity of directors until the selection of their successors are:

Name	Address
C. Ernest Davis	LaVerne, California
Lucile Davenport Weller	McFarland, California
J. E. Steinour	Los Angeles, California
Fred A. Flora	Los Angeles, California
L. E. Miller	Whittier, California

The number of persons named above shall constitute the number of directors of the corporation, until changed by an amendment to the by-laws increasing or decreasing the number of directors as may be desired.

## Article VI.

That the authorized number and qualifications of the members of the corporation which shall be all of one class, the property voting, election of directors, and other rights and privileges of the members, and the qualifications of directors shall be set forth in the by-laws of this corporation.

The Board of Directors shall constitute the members of the corporation. Vacancies on the Board of Directors shall be filled by The Elders Body of the Church of the Brethren of the Southern District of

## Joint Exhibit 8-H—(Continued)

California and Arizona, from nominations made by the Board of Directors, provided however, that any vacancy caused by death, resignation, or removal of Lucile Davenport Weller shall be filled by the Standing Committee of the Church of the Brethren at the time of the Church Conference. Said Standing Committee shall fill such vacancy from among the children of Levi M. Davenport, who have the qualifications specified by said Levi M. Davenport in a certain Trust Agreement filed with the corporation, and lacking such children the vacancy shall be filled from among the grandchildren of said Levi M. Davenport. It is the intention of this provision that a child or a grandchild of said Levi M. Davenport, as long as [141] any are living and have the necessary qualifications, shall be a member of said Board of Directors. When all of the children and grandchildren of Levi M. Davenport are dead or not qualified to serve as directors of this corporation, such vacancy shall be filled in the same manner as herein provided for filling other vacancies.

## Article VII.

That the by-laws of this corporation shall be adopted by the directors named in the Articles of Incorporation and may thereafter be amended or repealed by any means provided in the by-laws.

In Witness Whereof the persons who are to act in the capacity of first directors of the corporation

Joint Exhibit 8-H—(Continued)

have hereunto set their hands this 5 day of June, 1940.

/s/ C. ERNEST DAVIS,  
/s/ LUCILE DAVENPORT  
WELLER,  
/s/ J. E. STEINOUR,  
/s/ FRED A. FLORA,  
/s/ L. E. MILLER. [142]

State of California,  
County of Los Angeles—ss.

On this 19th day of June, 1940, before me, Jo Frances James a Notary Public in and for the County of Los Angeles, State of California, residing therein, duly commissioned and sworn, personally appeared Fred A. Flora, known to me to be the person whose name is subscribed to the foregoing instrument, and he duly acknowledged to me that he executed the same.

Witness my hand and official seal the day and year in this certificate first above written.

[Seal]                      JO FRANCES JAMES,  
Notary Public as aforesaid.

My Commission Expires January 2, 1944.

State of California,  
County of Kern—ss.

On this 5th day of June, 1940, before me, H. A. Bower a Notary Public in and for the County of Kern, residing therein, duly commissioned and

## Joint Exhibit 8-H—(Continued)

sworn, personally appeared Lucile Davenport Weller, known to me to be the person whose name is subscribed to the foregoing instrument, and she duly acknowledged to me that she executed the same.

Witness my hand and official seal the day and year in this certificate first above written.

[Seal]

H. A. BOWER,

Notary Public as aforesaid.

State of California,

County of Los Angeles—ss.

On this 17th day of June, 1940, before me, F. K. Bixler, a Notary Public in and for the County of Los Angeles, residing therein, duly commissioned and sworn, personally appeared J. E. Steinour, known to me to be the person whose name is subscribed to the foregoing instrument, and he duly acknowledged to me that he executed the same.

Witness my hand and official seal the day and year in this certificate first above written.

[Seal]

F. K. BIXLER,

Notary Public as aforesaid.

My Commission Expires March 15, 1944.

State of California,

County of Los Angeles—ss.

On this 25th day of June 1940, before me, Theo A. Davis a Notary Public in and for the County of Los Angeles, residing therein, duly commissioned



Joint Exhibit 8-H—(Continued)

and sworn, personally appeared C. Ernest Davis, known to me to be the person whose name is subscribed to the foregoing instrument, and he duly acknowledged to me that he executed the same.

Witness my hand and official seal the day and year in this certificate first above written.

[Seal]

THEO A. DAVIS,

Notary Public as aforesaid.

My commission Expires July 26, 1943. [144]

State of California,

County of Los Angeles—ss.

On this 20th day of June 1940, before me, C. H. Gates a Notary Public in and for the County of Los Angeles, residing therein, duly commissioned and sworn, personally appeared L. E. Miller, known to me to be the person whose name is subscribed to the foregoing instrument, and he duly acknowledged to me that he executed the same.

Witness my hand and official seal the day and year in this certificate first above written.

[Seal]

C. H. GATES,

Notary Public as aforesaid.

My Commission Expires February 25, 1943. [145]

## JOINT EXHIBIT 9-I

BY-LAWS OF THE DAVENPORT  
FOUNDATION

## Article I.

Section 1. Principal Office. The principal office for the transaction of business of the Foundation is hereby fixed at 674 Elliott Drive, in the City of Pasadena, County of Los Angeles, State of California.

The Board of Directors shall have power and authority to change said principal office from one location to another, and the Secretary shall note any such change opposite this Section.

## Article II.

Section 1. Directors. Subject to such limitations as may be prescribed by law all of the powers of the Foundation shall be exercised by, or under the authority of and the business and the affairs of the Foundation shall be controlled by the Board of Directors. Without prejudice to such general powers, but subject to the same limitations, it is hereby expressly [146] declared that the Board of Directors shall have the following powers:

First: To select and remove all the other officers, agents and employees of the Foundation, prescribe such powers and duties for them as may not be inconsistent with law, the Articles of Incorporation, or the By-laws, fix their compensation and require from them security for faithful service.

Second: To conduct, manage and control the affairs and business of the Foundation, and to make

## Joint Exhibit 9-I—(Continued)

such rules and regulations therefor not inconsistent with law, the Articles of Incorporation, or the By-Laws, as they may deem best.

Third: To borrow money and incur indebtedness and to cause to be issued therefor in the name of the Foundation, promissory notes, deeds of trust, mortgages, pledges, hypothecations, or other evidence of debt, and securities therefor. Subject to the limitations contained in the Articles of Incorporation.

Fourth: To appoint an Executive Committee and other committees and to delegate to the executive [147] committee any of the powers and authority of the Board in the management of the business and affairs of the Foundation. The Executive Committee shall be composed of two or more members of the Board of Directors.

Section 2. Number and Qualification of Directors. The authorized number of Directors shall be five (5), and their qualifications shall be as set forth in that certain Declaration of Trust dated May 23, 1939, under which The Davenport Foundation was operated prior to its incorporation.

Section 3. Election and Term of Office. The members of the first Board of Directors shall hold office until their successors are elected and qualified. They shall be elected and vacancies shall be filled as provided in that certain Declaration of Trust dated May 23, 1939, under which The Davenport Foundation was operated prior to its incorporation.

## Joint Exhibit 9-I—(Continued)

Section 4. Place of Meeting. Regular meetings of the Board of Directors shall be held at Pasadena, California, or at such other place as the Board of Directors shall designate by Resolution or by written consent of all members of the Board.

Section 5. Regular Meetings. The regular annual meeting of the Board of Directors shall be held on the third day of January at 9:30 o'clock A.M. of said day of each year, provided, however, should said day fall upon a legal holiday then said meeting shall be held at the same time on the next day thereafter ensuing which is not a legal holiday.

Other Regular Meetings. Other regular meetings of the Board shall be held upon call on the first Tuesday of April, July, and October of each year, at 9:30 o'clock a.m. of said day; provided, however, should said day fall upon a legal holiday, then said meeting shall be held at the same time on the next day thereafter ensuing, which is not a legal holiday. Notice of all such regular meetings of the Board of Directors is hereby dispensed with.

Section 6. Special Meetings. Special meetings of the Board of Directors for any purpose or purposes shall be called at any time by the President, or if he be absent or unable, or refuses to act by any Vice President or by two Directors. Written notice of the time and place of special meetings shall be delivered personally [149] to the Directors or sent to each Director by mail or other form of written communication, charges prepaid, addressed to him at his address as it is shown upon the records of the



## Joint Exhibit 9-I—(Continued)

Foundation, or if it is not so shown on such records or is not readily ascertainable, at the place in which the meetings of the Directors are regularly held. In case such notice is mailed, or telegraphed, it shall be deposited in the United States Mail, in any place in the County of Los Angeles, or delivered to any Telegraph Company in any place in Los Angeles County, California, at least three days prior to the time of the holding of the meeting. In case such notice is delivered as above provided, it shall be so delivered at least three days prior to the time of the holding of the meeting. Such mailing, telegraphing or delivery as above provided shall be due, legal and personal notice to such Directors.

Section 7. Notice of Adjournment. Notice of the time and place of holding an adjourned meeting need not be given to absent Directors if the time and place be fixed at the meeting adjourned.

Section 8. Entry of Notice. Whenever any Director has been absent from any special meeting of the Board of Directors, an entry in the minutes to the effect that notice has been duly given shall be conclusive and incontrovertible evidence that due notice of such special meeting was given to such Director, as required by law and the By-laws of the Foundation.

Section 9. Waiver of Notice. The transactions of any meeting of the Board of Directors, however called and noticed or wherever held, shall be as valid as though had at a meeting duly held after regular call and notice, if a quorum be present, and

## Joint Exhibit 9-I—(Continued)

if, either before or after the meeting, each of the Directors not present sign a written waiver of notice or a consent to holding such meeting or an approval of the minutes thereof. All such waivers, consents or approvals shall be filed with the records or made a part of the minutes of the meeting.

Section 10. Quorum. A majority of the authorized number of Directors shall be necessary to constitute a quorum for the transaction of business, except to adjourn as hereinafter provided. Every act or decision done or made by a majority of the Directors [151] present at a meeting duly held at which a quorum is present shall be regarded as the act of the Board of Directors, unless a greater number be required by law.

Section 11. Adjournment. A quorum of the Directors may adjourn any Directors' meeting to meet again at a stated day and hour; provided, however, that in the absence of a quorum, a majority of the Directors present at any Directors' meeting, either regular or special, may adjourn from time to time until the time fixed for the next regular meeting of the Board.

Section 12. Fees and Compensation. Directors shall not receive any stated salary for their services as Directors, but, by resolution of the Board, a fixed fee, with or without expenses of attendance, may be allowed for attendance at each meeting. Nothing herein contained shall be construed to preclude any Director from serving the Foundation in any other capacity as an officer, agent, employee, or otherwise, and receiving compensation therefor.

## Joint Exhibit 9-I—(Continued)

## Article III.

Section 1. Officers. The officers of the Foundation shall be a President, a Vice President, a Secretary, [152] and a Treasurer. The Foundation may also have, at the discretion of the Directors, a chairman of the Board, one or more additional Vice Presidents, one or more Assistant Secretaries, one or more Assistant Treasurers, and such other officers as may be appointed in accordance with the provisions of Section 3 of this Article. All officers must be Directors. One person may hold two or more offices, except those of President and Secretary.

Section 2. Election. The officers of the Foundation, except such officers as may be appointed in accordance with the provisions of Section 3 or Section 5 of this Article, shall be chosen annually by the Board of Directors, and each shall hold his office until he shall resign or shall be removed or otherwise disqualified to serve, or his successor shall be elected and qualified.

Section 3. Subordinate Officers, Etc. The Board of Directors may appoint such other officers as the business of the Foundation may require, each of whom shall hold office for such period, have such authority, and perform such duties as are provided in the By-laws or as the Board of Directors may from time to time determine. [153]

Section 4. Removal and Resignation. Any officer may be removed, either with or without cause, by a majority of the Directors at the time in office,

## Joint Exhibit 9-I—(Continued)

at any regular or special meeting of the Directors, or except in case of an officer chosen by the Board of Directors, by any officer upon whom such power of removal may be conferred by the Board of Directors.

Any officer may resign at any time by giving written notice to the Board of Directors or to the President, or to the Secretary of the Foundation. Any such resignation shall take effect at the date of the receipt of such notice or at any later time specified therein; and, unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

Section 5. Vacancies. A vacancy in any office because of death, resignation, removal, disqualification or any other cause, shall be filled in the manner prescribed in the By-laws for regular appointments to such office.

Section 6. Chairman of the Board. The chairman of the Board, if there shall be such an officer, shall, if present, preside at all meetings of the Board of Directors, or prescribed by the By-laws.

Section 7. President. Subject to such supervisory powers, if any, as may be given by the Board of Directors to the chairman of the Board, if there be such an officer, the president shall be the chief executive officer of the Foundation and shall, subject to the control of the Board of Directors, have general supervision, direction and control of the business and officers of the Foundation. He shall preside at all meetings of the Directors in the ab-



## Joint Exhibit 9-I—(Continued)

sence of the chairman of the Board. He shall be ex-officio a member of all the standing committees including the executive committee, if any, and shall have the general powers and duties of management usually vested in the office of president of a Foundation, and shall have such other powers and duties, as may be prescribed by the Board of Directors or by the By-laws.

Section 8. Vice President. In the absence or disability of the president, the vice-presidents in order of their rank as fixed by the Board of Directors, or if not ranked, the vice-president designated by the Board of Directors, shall perform all the duties of the President, and when so acting shall have all the powers of, and be subject to all the restrictions upon, the president. The vice-presidents [155] shall have such other powers and perform such other duties as from time to time may be prescribed for them respectively by the Board of Directors or the By-laws.

Section 9. Secretary. The secretary shall keep, or cause to be kept, a book of minutes at the principal office or such other place as the Board of Directors may order, of all meetings of Directors, with the time and place of holding, whether regular or special, and if special, how authorized, the notice thereof given, the names of those present at directors' meetings, and the proceedings thereof.

The Secretary shall give, or cause to be given notice of all the meetings of the Board of Directors required by the By-laws or by law to be given,

## Joint Exhibit 9-I—(Continued)

and shall have such other powers and perform such other duties as may be prescribed by the Board of Directors or the By-laws.

Section 10. Treasurer. The treasurer shall keep and maintain, or cause to be kept and maintained, adequate and correct accounts of the property and business transactions of the Foundation, including accounts of its assets, liabilities, receipts, disbursements, gains, losses, capital, and surplus. [156] The books of account shall at all times be open to inspection by any Director.

The treasurer shall deposit all moneys and other valuables in the name and to the credit of the Foundation with such depositaries as may be designated by the Board of Directors. He shall disburse the funds of the Foundation as may be ordered by the Board of Directors, shall render to the president and Directors, whenever they request it, an account of all of his transactions as treasurer and of the financial condition of the corporation, and shall have such other powers and perform such other duties as may be prescribed by the Board of Directors or the By-laws.

## Article IV.

## Miscellaneous

Section 1. Checks, Drafts, Etc. All checks, drafts or other orders for payment of money, notes or other evidences of indebtedness, issued in the name of or payable to the Foundation, shall be signed or endorsed by such person or persons and

## Joint Exhibit 9-I—(Continued)

in such manner as, from time to time, shall be determined by resolution of the Directors. [157]

Section 2. Annual Report. The Board of Directors of the Foundation shall cause to be sent to the District Conference of the Church of the Brethren of the Southern District of California and Arizona, not later than twenty days before the Annual meeting of said District Conference, an annual report of the business of the Foundation.

Section 3. Contract, Etc., How Executed. The Board of Directors, except as in the By-laws otherwise provided, may authorize any officer or officers, agent or agents, to enter into any contract or execute any instrument in the name of and on behalf of the Foundation, and such authority may be general or confined to specific instances; and unless so authorized by the Board of Directors, no officer, agent, or employee shall have any power or authority to bind the Foundation by any contract or engagement or to pledge its credit or to render it liable for any purpose or to any amount.

Section 4. The provisions of the Declaration of Trust herein referred to, so far as the same may be applicable, shall govern the affairs of the Foundation.

Section 5. The Foundation may receive gifts of additional property, subject to such terms and conditions [158] as the donor may make, provided said terms and conditions are acceptable to the Board of Directors.

Section 6. Seal. This corporation shall have a

## Joint Exhibit 9-I—(Continued)

common seal, circular in form, having the following words and figures thereon:

The Davenport Foundation  
Incorporated July 8, 1940,  
Pasadena, California.

## Article V.

## Amendments

Section 1. Power of Directors. New By-laws may be adopted or these By-laws may be amended or repealed by the Board of Directors. [159]

Know All Men by These Presents:

That we, the undersigned, being all of the members and incorporators of the Davenport Foundation, a corporation organized under and existing by virtue of the laws of the State of California, and having its principal place of business in the City of Pasadena, County of Los Angeles, State of California, hereby assent to the foregoing by-laws contained on pages 1 to 14, both inclusive, of this book of by-laws, and we hereby adopt the same as and for the by-laws of said corporation.

In Witness Whereof we have hereunto subscribed our names this 5th day of September, 1940.

C. ERNEST DAVIS,  
LUCILE DAVENPORT  
WELLER,  
J. E. STEINOUR,  
FRED A. FLORA,  
L. E. MILLER. [160]



Joint Exhibit 9-I—(Continued)

Certificate of Secretary

I, the undersigned, do hereby certify:

(1) That I am the duly elected and acting secretary of the Davenport Foundation, a corporation, and

(2) That the foregoing By-laws, comprising Fourteen (14) pages constitute the original By-laws of said Foundation as duly adopted at the first meeting of the Board of Directors thereof duly held Thursday, September 5th, 1940.

In Witness Whereof, I have hereunto subscribed my name this 5th day of September, 1940.

FRED A. FLORA,  
Secretary. [161]

JOINT EXHIBIT 10-J

Motion by Mrs. Weller, seconded by Mr. Steinour, and carried, the following resolution was adopted:

Whereas Levi M. Davenport and Barbara N. Davenport, his wife, heretofore conveyed certain property to the La Verne College, which was received by said College under a Declaration of Trust dated the 23rd day of May, 1939, which Declaration of Trust was designated as The Davenport Foundation, and

Whereas on July 8th, 1940, said Foundation was incorporated under the laws of the State of California, and the incorporators, the first Board of Directors of said corporation, have met and organized themselves as a Board of Directors with the necessary and proper officers pursuant to the by-

laws theretofore adopted by the members of said corporation, and

Whereas one of the purposes of organizing said corporation was to receive and hold title to said property heretofore conveyed to said La Verne College, and the existence of the Davenport Foundation, an unincorporated association which has heretofore managed and controlled the operation of said property, may be dissolved upon the transfer of said property to said corporation known as The Davenport Foundation, and

Whereas the Board of Directors of said unincorporated Foundation has requested that all of the property held by La Verne College under said Declaration of Trust be transferred to The Davenport Foundation, a corporation, [162]

Now Therefore Be it resolved that La Verne College be, and it is hereby instructed to convey to The Davenport Foundation, a corporation, all of the property and assets which La Verne College now holds under the said Declaration of Trust. Such conveyances and transfers shall be made subject to that certain Declaration of Trust of May 23rd, 1939, designated The Davenport Foundation, an unincorporated association, and the acceptance thereof by this corporation known as The Davenport Foundation shall be a recognition of the fact that the assets so transferred are subject to and accepted by this corporation, subject to the terms and provisions of said Declaration of Trust.

Adopted September 5, 1940. [163]

JOINT EXHIBIT 11-K

GRANT DEED

CORPORATION

Recorded February 20, 1941, 8:00 A.M. Book 489, Page 591, Official Records Riverside County, California.

La Verne College, a corporation, organized under the laws of the State of California, with its principal place of business at LaVerne, California, in consideration of Ten Dollars, to it in hand paid, the receipt of which is hereby acknowledged, does hereby Grant to the Davenport Foundation, a corporation organized under the laws of the State of California, with its principal place of business at Pasadena, California, all that property in the County of Riverside, State of California, described as:

\* \* \* \* \*

Actual consideration less than One Hundred Dollars.

In Witness Whereof, the above mentioned corporation has caused this deed to be duly executed and its corporate name to be subscribed hereto by its President and attested by its Secretary, who has hereunto affixed its corporate seal, this 8th day of October, 1940.

[Corporate Seal]

LA VERNE COLLEGE,  
By EDGAR ROTHROCK,  
President.

Attest:

J. C. BRANDT,  
Secretary. [164]

\* \* \* \* \*

## JOINT EXHIBIT 12-L

## CORPORATION GRANT DEED

Recorded October 24, 1940, 2:27 P.M. Book 17911,  
Page 202, Official Records Los Angeles County, Cali-  
fornia.

La Verne College, a corporation organized under  
the laws of the State of California, with is prin-  
cipal place of business at LaVerne, California, in  
consideration of Ten Dollars, to it in hand paid,  
receipt of which is hereby acknowledged, does  
hereby grant to The Davenport Foundation, a cor-  
poration organized under the laws of the State of  
California, with its principal place of business at  
Pasadena, California, the real property in the  
County of Los Angeles, State of California, de-  
scribed as follows:

\* \* \* \* \*

Actual consideration less than \$100.00.

In Witness Whereof, said Corporation has caused  
its corporate name and seal to be affixed hereto and  
this instrument to be executed by its President and  
Secretary thereunto duly authorized, this 8th day  
of October, 1940.

[Corporate Seal]

LA VERNE COLLEGE,  
By EDGAR ROTHROCK,  
President,  
By J. C. BRANDT,  
Secretary. [165]



## JOINT EXHIBIT 13-M

## GRANT DEED

Recorded July 14, 1941, 11:33 A.M. Book 18464,  
Page 346, Official Records Los Angeles County,  
California.

In Consideration of less than 100.00, receipt  
of which is acknowledged, Levi M. Davenport, some-  
times known as L. M. Davenport, a married man,  
as his separate property, whose wife's name is  
Barbara N. Davenport, whose permanent address is  
....., does hereby grant to The Davenport Foun-  
dation, a corporation, organized under the laws of  
the State of California, with its principal place of  
business at Pasadena, California, whose permanent  
address is ....., the real property in the City of  
Pasadena County of Los Angeles, State of Califor-  
nia, described as:

\* \* \* \* \*

Dated this 31st day of May, 1941.

LEVI M. DAVENPORT,  
BARBARA N. DAVENPORT.

## JOINT EXHIBIT 14-N

## ANNUITY AGREEMENT

Recorded July 14, 1941, 11:33 a.m., Book 18548,  
Page 326, Official Records, Los Angeles County,  
California.

This Agreement Made and entered into this 23rd  
day of June, 1941, by and between The Davenport  
Foundation, a corporation, organized under and  
existing by virtue of the laws of the State of Cali-  
fornia, and having its principal office for the trans-

action of business located in the City of Pasadena, County of Los Angeles, State of California, the party of the first part, hereinafter called Donee, and L. M. Davenport and Barbara N. Davenport, husband and wife, of Pasadena, California, the parties of the second part, hereinafter called Donors.

Witnesseth: That

Whereas, contemporaneously with the execution of this agreement the Donors have conveyed to the Donee that certain real property situate, lying, and being in the City of Pasadena, County of Los Angeles, State of California, and more particularly described as follows, to wit:

Lots 50 and 49 of Tract No. 360, Oak Knoll, as per map recorded in Book 15, Page 22 of Maps, in the office of the County Recorder of said County. Except from Lot 49 that portion described as follows: Starting at the Southeast corner of said Lot 49; thence North along line of Oak Knoll Avenue 100 feet; thence West to a point in West line of said Lot, 70 feet distant from Southwest corner of said Lot; thence South along said West line of said Lot, 70 feet to Southwest corner of said Lot; thence East 138.65 feet, more or less, along South line of said Lot to point of beginning.

Whereas, said Donee has paid no consideration for said property and the Donors have conveyed said property upon certain terms and conditions to which conditions the Donee has consented, all of which said conditions are contained herein. [167]

Now Therefore, the Donee in consideration of the transfer to it of said property does hereby agree as follows:

1. To accept and does hereby accept said property subject to the right of the Donors and the survivor of them to the use thereof for and during the term of their and each of their natural lives. If, however, the Donor L. M. Davenport should predecease the Donor, Barbara N. Davenport, such right shall terminate in the event said Barbara N. Davenport does not desire to live in or upon said premises. The Donee in consideration of the transfer to it of said property and other valuable consideration agrees to pay to Lucile Davenport Weller, daughter of the Donor, L. M. Davenport, the sum of \$100.00 per month, on or before the 5th day of each and every month, retroactive to January 1st, 1941, in monthly installments for and during the term of her natural life.

2. Upon the death of said Lucile Davenport Weller, to pay to Dorothy Mae Weller, granddaughter of the Donor, L. M. Davenport, and daughter of Lucile Davenport Weller, the sum of \$100.00 per month for and during the term of her natural life provided, however, that in the event she should marry and her gross income from other sources together with that of her husband should equal \$300.00 per month, then and thereupon said monthly sum shall be reduced to \$50.00 per month, and in the event that their gross combined incomes as aforesaid should equal \$500.00 per month said payment shall cease and this [168] annuity terminate and

said property and the income thereupon shall belong to said Donee free and clear of all of the conditions herein placed thereon to be used for the general purposes of the Foundation. It is understood and agreed by and between the Donors and the Donee that the annuity income herein provided shall not be assignable nor shall the annuitants or either of them have any power to sell, incumber or anticipate the payments of said annuity or annuities and that the same shall not in any manner whatsoever be liable for the payment of any debt she may now owe or hereafter incur; that after the death of the Donors, or in the event that Barbara N. Davenport should not occupy said premises after the death of said L. M. Davenport, the Donee may sell or exchange said premises.

This Agreement shall be binding upon the heirs, executors, and administrators of the Donors and the successors and assigns of the Donee.

THE DAVENPORT  
FOUNDATION,

By C. ERNEST DAVIS,  
President.

[Corporate Seal]

By FRED A. FLORA,  
Secretary.

L. M. DAVENPORT,  
BARBARA N. DAVENPORT.



State of California,  
County of Los Angeles—ss.

On this 3rd day of July, A.D. 1941, before me, Fred L. Merrill, a Notary Public in and for said County and State, personally appeared Fred A. Flora, L. M. Davenport & Barbara N. Davenport, known to me to be the persons whose names are subscribed to the within Instrument, and acknowledged to me that they executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year in this certificate first above written.

[Notarial Seal] FRED L. MERRILL,

Notary Public in and for Said  
County and State.

My Commission Expires March 27, 1945.

State of California,  
County of Los Angeles—ss.

On this 23rd day of June, 1941, before me, Theo. A. Davis, a Notary Public in and for said County, personally appeared C. Ernest Davis known to me to be the person whose name is subscribed to the within instrument and acknowledged that he executed the same.

Witness my hand and official seal.

[Notarial Seal] THEO. A. DAVIS,

Notary Public in and for Said  
County and State. [170]

## JOINT EXHIBIT 15-O

## GRANT DEED

Recorded July 14, 1941, 11:33 a.m., Book 18614, Page 64, Official Records, Los Angeles County, California.

In Consideration of Less than \$100.00, receipt of which is acknowledged, Levi M. Davenport, sometimes known as L. M. Davenport, and Barbara N. Davenport, his wife, whose permanent address is . . . . ., do hereby grant to The Davenport Foundation, a corporation, whose permanent address is . . . . ., the real property in the City of Los Angeles, County of Los Angeles, State of California, described as:

\* \* \* \* \*

Dated this 31st day of May, 1941.

LEVI M. DAVENPORT,  
BARBARA N. DAVENPORT.

## JOINT EXHIBIT 16-P

## ANNUITY AGREEMENT

Recorded July 14, 1941, 11:33 a.m., Book 18580, Page 185, Official Records, Los Angeles County, California.

This Agreement Made and entered into this 23rd day of June, 1941, by and between The Davenport Foundation, a corporation, organized and existing by virtue of the laws of the State of California, and having its principal office for the transaction of business located in the City of Pasadena, County of Los Angeles, State of California, the party of

the first part, hereinafter called Donee, and L. M. Davenport and Barbara N. Davenport, husband and wife, of Pasadena, California, the parties of the second part, hereinafter called Donors.

Witnesseth: That

Whereas, contemporaneously with the execution of this agreement, the Donors have conveyed to the Donee that certain real property situate, lying, and being in the City of Los Angeles, County of Los Angeles, State of California, and more particularly described as follows, to wit:

Beginning at a point in the Southerly line of First Street distant two hundred and seventy-sevenths hundredths (200.77) feet Westerly from its intersection with the Easterly line of Lot "15d" of the Subdivision of the Garden of J. Murat, as per map recorded in Book 10, Page 8, Miscellaneous Records of said County; thence South  $39^{\circ} 51'$  West (12) feet; thence Westerly on a line parallel with and distant six and one-half ( $6\frac{1}{2}$ ) feet Southerly from the Southerly wall (and the prolongation Easterly of the Southerly line thereof) of the brick building formerly owned by Joseph Murat, shown on map accompanying deed recorded in Book 10, Page 111 of Deeds, Records of said County, eighty-nine (89) feet more or less, to a point in the Easterly line of San Pedro Street; thence Northerly along said street line, thirty-nine and two-twelfths ( $39\frac{2}{12}$ ) feet to a point in said street line.

distant two (2) feet Northerly from the prolongation Westerly of the line of the Northerly wall of said building; thence Easterly on a straight line sixty-nine and one-half ( $69\frac{1}{2}$ ) feet, more or less, to a point in the Southerly line of First Street, distant forty-two and twenty-four one-hundredths ( $42\frac{24}{100}$ ) feet Westerly from the point of beginning; thence Easterly [172] along said Southerly line of First Street to the point of beginning. Together with all right, title and interest of the Grantors herein and to those portions of San Pedro and First Streets immediately adjoining and adjacent to the premises hereinbefore described, and

Whereas, said Donee has paid no consideration for said property and the Donors have conveyed said property upon certain terms and conditions to which conditions the Donee has consented, all of which said conditions are contained herein.

Now Therefore, the Donee in consideration of the transfer to it of said property does hereby agree as follows:

1. To accept and does hereby accept said property subject to the right of the Donor, L. M. Davenport to receive the net income derived and to be derived therefrom for and during the term of his natural life, and to the right reserved by the said Donor to designate in writing, during his lifetime, the disposition or use of said net income, for a period not to exceed ten years, after the death of said Donor, L. M. Davenport.



2. Upon the death of Donor L. M. Davenport and the expiration of the period during which, the donor may have in writing designated the use or disposition of the net income (not exceeding ten years) said property and the income therefrom shall belong to said Donee free and clear of all the conditions herein placed thereon, to be used for the General purposes of The Foundation, the donee herein.

This Agreement shall be binding upon the heirs, executors, and administrators of the Donors and the successors and assigns of the Donee.

THE DAVENPORT  
FOUNDATION,

By C. ERNEST DAVIS,  
President.

By FRED A. FLORA,  
Secretary.

[Corporate Seal]

By L. M. DAVENPORT,  
By BARBARA N. DAVENPORT.

State of California,  
County of Los Angeles—ss.

Subscribed and sworn to this 23rd day of June,  
1941, by C. Ernest Davis.

[Notarial Seal]

/s/ THEO A. DAVIS,

Notary Public in and for Said  
County.

My Commission Expires July 26, 1943.

State of California,  
County of Los Angeles—ss.

On this 3rd day of July, A.D. 1941, before me, Fred L. Merrill, a Notary Public in and for said County and State, personally appeared Fred A. Flora, L. M. Davenport & Barbara N. Davenport, known to me to be the persons whose names are subscribed to the within Instrument, and acknowledged to me that they executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year in this certificate first above written.

[Notarial Seal] FRED L. MERRILL,

Notary Public in and for Said  
County and State.

My Commission Expires March 27, 1945. [174]

# JOINT EXHIBIT 17-Q

## THE DAVENPORT FOUNDATION

Taxable Net Income Per Revenue Agent's  
Letter of March 1, 1946, and Book Net Income

Income	1940	1941	1942	1943	1944
Interest .....	\$ 517.45	\$ 822.28	\$ 1,934.26	\$ 3,705.98	\$ 3,254.49
Rents (Gross) .....	6,986.54	13,894.77	15,182.35	17,337.38	16,540.06
Royalties (Oil) .....	125.33	220.54	224.35	201.73	197.93
Net Short-term Capital Gain.....		645.72			
Net Long-term Capital Gain.....	(61.60)	681.27	329.60	1,517.65	2,759.49
Total Income .....	\$7,477.72	\$16,264.58	\$17,670.56	\$22,762.74	\$22,751.97

## Deductions

Rent and Miscellaneous.....	\$ 351.56	\$ 653.04	\$ 786.14	\$ 1,153.14	\$ 930.93
Repairs and Property					
Maintenance .....	802.40	2,403.26	1,500.12	1,743.87	2,273.79
Interest .....	278.48	155.28	26.67	106.69	
Taxes .....	1,348.95	3,204.84	2,841.56	3,079.29	4,140.20
Contributions .....	165.87	346.71	467.68	468.29	576.93
Depreciation .....	1,252.22	2,432.47	2,592.47	2,793.14	2,286.23
Other Deductions.....	126.63	480.78	569.88	4,520.70	1,582.27
Total Deductions.....	\$4,326.11	\$ 9,677.08	\$ 8,784.52	\$13,865.12	\$11,790.35
Net Income (IRA) .....	\$3,151.61	\$ 6,587.50	\$ 8,886.04	\$ 8,897.62	\$10,961.62
Unallowable Contributions.....	\$1,369.31	\$ 3,613.29	\$ 3,500.26	\$ 4,291.36	\$ 5,600.07
Book Net Income.....	\$1,782.30	\$ 2,974.21	\$ 5,385.78	\$ 4,606.26	\$ 5,361.55
Amounts Paid to Members of Davenport Family from Foundation					
Years 1940 to 1944, Inclusive					
Lucille Weller.....	*\$1,000.00	\$ 1,200.00	\$ 1,200.00	\$ 1,200.00	\$ 1,200.00
Homer Davenport.....		*625.00			



The Tax Court of the United States  
Docket No. 10,427

THE DAVENPORT FOUNDATION,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent,

PRAECIPE FOR TRANSCRIPT

To the Clerk of the Tax Court of the United States:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, copies duly certified as correct of the following documents and records in the above entitled cause in connection with the Petition for Review by the said Circuit Court of Appeals for the Ninth Circuit, heretofore filed by the above named petitioner:

1. Docket entries of the proceedings before the Tax Court of the United States.
2. Original petition.
3. Answer to original petition.
4. Amended petition.
5. Answer to amended petition.
6. Memorandum, Findings of Fact and Opinion of the Tax Court promulgated December 24, 1947.
7. Decision of the Tax Court entered on December 29, 1947. [176]
8. Petition for Review filed on March 24, 1948.
9. Notice of filing Petition for Review filed on March 24, 1948.
10. Statement of Evidence approved and filed on April 19, 1948, and exhibits attached.

11. This Praeipe for Record.
12. Notice of filing this Praeipe for Record and the admission of service thereof.

Said transcript to be prepared as required by law and the rules of the United States Circuit Court of Appeals for the Ninth Circuit.

/s/ MELVIN D. WILSON,  
Attorney for Petitioner.

Service of a copy of this Praeipe for Record is hereby admitted this 19th day of April, 1948.

/s/ CHARLES OLIPHANT, OWS  
Chief Counsel, Bureau of Internal Revenue, Attorney for Respondent.

[Endorsed]: Filed April 19, 1948. [177]

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[Title of Tax Court and Cause.]

### CERTIFICATE

I, Victor S. Mersch, clerk of the Tax Court of the United States do hereby certify that the foregoing pages, 1 to 177, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praeipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 20th day of April, 1948.

[Seal] /s/ VICTOR S. MERSCH, EMT  
Clerk, the Tax Court of  
the United States.

[Endorsed]: No. 11912. United States Circuit Court of Appeals for the Ninth Circuit. The Davenport Foundation, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review a Decision of The Tax Court of the United States.

Filed April 26, 1948.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Circuit Court of Appeals  
for the Ninth Circuit.

In the United States Circuit Court of Appeals  
for the Ninth Circuit

No. 11912

THE DAVENPORT FOUNDATION,

Appellant,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Appellee.

STATEMENT OF POINTS ON WHICH  
APPELLANT INTENDS TO RELY AND  
DESIGNATION OF PARTS OF THE  
RECORD NECESSARY FOR CONSID-  
ERATION

To the Honorable Paul P. O'Brien, Clerk of the  
United States Circuit Court of Appeals for the  
Ninth Circuit:

Petitioner adopts as its points on appeal the  
assignments of error included in the petition for  
review within the transcript of record.

The petitioner designates for printing, the entire  
transcript of the record.

Dated May 3, 1948.

/s/ MELVIN D. WILSON,  
Attorney for Appellant.

[Endorsed]: Filed May 4, 1948.



No. 11,912

IN THE

United States Circuit Court of Appeals  
FOR THE NINTH CIRCUIT

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THE DAVENPORT FOUNDATION,

*Petitioner,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

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BRIEF ON BEHALF OF PETITIONER.

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MELVIN D. WILSON,

819 Title Insurance Building, Los Angeles 13,

*Counsel for Petitioner.*

FILED

JUL 13 1948

PAUL P. O'BRIEN,

CLERK



## TOPICAL INDEX

	PAGE
Statement of the case.....	1
Question involved .....	2
Statement .....	3
Specification of errors relied upon.....	12
Statutes involved .....	13
Summary of argument.....	14
Argument .....	17
Petitioner is exempt from tax under Section 101(6) of the Internal Revenue Code.....	17
(A) The reservation, by a donor of property to an other- wise exempt corporation, of an interest in property or an annuity payable to the donor or others, does not destroy the exemption of the donee.....	18
(B) All the payments to be made by petitioner to donor and his family were required by reservations and ex- ceptions from the properties contributed to petitioner by donor .....	23
(C) All of petitioner's authorized contributions were made for charitable, religious and educational work.....	29
(D) Petitioner is to be repaid for any expenditures made for unauthorized purposes.....	31

### II.

In the alternative petition was a corporation organized for the exclusive purpose of holding title to property, collecting income therefrom and turning over the entire amount thereof, less expenses, to an organization which itself is exempt from income tax.....	33
---	----

### III.

Petitioner is exempt from declared value excess profits tax....	35
Summary .....	36

## TABLE OF AUTHORITIES CITED

CASES	PAGE
Blair v. Commissioner, 300 U. S. 5.....	24
Emerit v. Baker, Inc. v. Commissioner, 40 B. T. A. 555, Acq. 1940-1 C. B. 1.....	19
Home Oil Mill, et al. v. Willingham, 68 Fed. Supp. 525; dis- missed Jan. 9, 1947, Prentice-Hall Fed. Tax Serv., par. 72304 .....	21
Laughlin, Homer, Estate of, 8 T. C. 33.....	24
Lederer v. Stockton, 260 U. S. 3.....	18
Pasadena Methodist Foundation v. Commissioner, T. C. Memo. Dec., Docket Nos. 109667, 109668, Oct. 11, 1943, C. C. H. Dec. 13, 544M.....	21
Whitehead, J. B., Estate of, v. Commissioner, 3 T. C. 40; aff'd 147 F. (2d) 977.....	20

### STATUTES

Internal Revenue Code, Sec. 23(o)(2).....	22
Internal Revenue Code, Sec. 101 .....	13, 35
Internal Revenue Code, Sec. 101(6).....	2, 9, 11, 13, 15, 31, 33, 35, 36
Internal Revenue Code, Sec. 101(8).....	35
Internal Revenue Code, Sec. 101(14).....	2, 13, 14, 16, 31, 33, 35, 36
Internal Revenue Code, Sec. 600 .....	2, 13, 35, 36
Internal Revenue Code, Sec. 1200.....	2, 13, 35, 36
Internal Revenue Code, Sec. 1201(a)(1) .....	2, 13, 35, 36
Revenue Act of 1926, Sec. 214(a)(10).....	22

### TEXTBOOKS

26 Corpus Juris Secundum, p. 457.....	25
Cumulative Bulletin, June 1933, p. 56, Gen. Counsel Memo. 11,817 .....	33
Cumulative Bulletin 1945, 114, I. T. 3707.....	21, 22
Cumulative Bulletin II-2, 151, I. T. 1776.....	21
Cumulative Bulletin VII-1, 90, I. T. 2397.....	21, 22
Cumulative Bulletin VII-1, 90, Gen. Counsel Memo. 3016.....	21



No. 11,912

IN THE

**United States Circuit Court of Appeals**  
FOR THE NINTH CIRCUIT

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THE DAVENPORT FOUNDATION,

*Petitioner,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

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**BRIEF ON BEHALF OF PETITIONER.**

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**Statement of the Case.**

This case comes before the Court on a petition for a review of a decision and order of The Tax Court of the United States determining deficiencies in the Federal taxes of petitioner, as follows:

Year	Income Tax	Declared Value Excess-Profits Tax
1940	\$ 468.02	\$ ———
1941	1,415.13	409.20
1942	2,292.63	300.11
1943	2,272.00	86.30
1944	2,804.44	—————

### Question Involved.

The question involved is whether petitioner was exempt from Federal corporate income tax for the years 1940 to 1944, inclusive, and declared value excess profits tax, for the years 1941 to 1943, inclusive, under the provisions of Section 101(6) and Sections 600, 1200, 1201(a)(1) of the Internal Revenue Code, or in the alternative under the provisions of Section 101(14) and Sections 600, 1200, 1201(a)(1) of the Internal Revenue Code.

The petitioner contends, (1) that it was exempt for the years mentioned above, as it was a corporation organized and operated exclusively for religious, charitable or educational purposes, no part of the net earnings of which inured to the benefit of any private shareholder or individual and no substantial part of the activities of which was carrying on propaganda or otherwise attempting to influence legislation, or (2) in the alternative, was exempt as it was a corporation organized for the exclusive purpose of holding title to property, collecting income therefrom and turning over the entire amount thereof, less expenses, to an organization which itself is exempt from income tax.

The respondent contends that a substantial part of petitioner's income inured to the benefit of private individuals, or in the alternative, that not all of petitioner's income was turned over to organizations which themselves were exempt from income tax, and hence the petitioner was not exempt from income or declared value excess profits tax.

The Tax Court denied the petitioner's contentions, and held that it was not exempt from income and declared value excess profits tax.

### Statement.

The facts are not in dispute as written and documentary evidence was introduced as joint exhibits by the respective parties and the respondent introduced no oral testimony.

Petitioner was incorporated July 8, 1940 under the laws of California as a non-profit corporation [Tr. 75], for the stated purpose "To act as Trustee under Christian Educational, Charitable, Eleemosynary, and other charitable trusts" [Tr. 114]. Specifically, petitioner was to replace LaVerne College as trustee of a trust created on May 23, 1939 by Levi M. Davenport [Tr. 58]. On September 5, 1940 the Board of Trustees of the trust, also called The Davenport Foundation, adopted a resolution which provided that all of the property in the trust created by Levi M. Davenport was to be transferred to The Davenport Foundation, a corporation, subject to the terms of the declaration of trust and that the acceptance of the assets by the corporation was to be a recognition of the fact that the assets so transferred were subject to and accepted by the corporation subject to the terms and provisions of the declaration of trust [Tr. 135-6]. Petitioner's Articles of Incorporation [Tr. 120], and its By-Laws, provided that vacancies on the Board of Directors should be filled from persons having qualifications specified in the said trust created by Levi M. Davenport on May 23, 1939.

On May 23, 1939, Levi M. Davenport executed an irrevocable transfer in trust of substantially all of his real and personal property [Tr. 34], to LaVerne College, a corporation, as trustee with Davis, Weller, Steinour, Flora & Miller as the Board of Trustees of the trust [Tr. 84-97]. On the same day the Board of Trustees adopted

by-laws for the trust [Tr. 98-108]. Also on May 23, 1939 Levi M. Davenport transferred to the trust, subject to certain reservations and exceptions, property having a value of \$261,884.00 [Tr. 76]. On June 1, 1939 Barbara N. Davenport, wife of Levi M. Davenport, transferred to the trust, subject to certain reservations, two parcels of real estate having a value of \$8,500.00 [Tr. 78, 108 to 110, incl.].

The trust established by Levi M. Davenport and his wife was created for religious, charitable and educational purposes. The management of the trust was vested in a Board of Trustees which was subject to the control of the Elders Body of the Church of the Brethren of the District of Southern California and Arizona. Members of the Board of Trustees were required to be persons who subscribed to certain fundamental religious doctrines set forth in the declaration of trust [Tr. 84-97].

Certain reservations were made from the transfers of property to the trust. \$400.00 per month was reserved to Levi M. Davenport for his life. He also reserved for his lifetime the right to the use and occupation, rent free, of the home then occupied by him at 674 Elliott Drive, Pasadena, California, or some other home of similar rental value. The donor also excepted from the transfer, the right, subject to the discretion of the Board of Trustees, (1) to have \$100.00 per month paid to J. R. Davenport, the brother of Levi M. Davenport, for his support and maintenance, and (2) also subject to the discretion of the Board of Trustees, a portion of the trust income for the care of any child of Levi M. Davenport who might "come to want." Neither the \$400.00 per month nor any amount for the brother or children of Levi M. Davenport has ever been paid [Tr. 62, 64, 65, 150].



The trust was required to pay \$300.00 per month to LaVerne College, a corporation, for the purpose of establishing a Department of Philosophy and Religion; at the discretion of the Board, \$300.00 per year to the American Bible Society, New York City; such annuities as might be agreed upon between the Board of Trustees and the annuitants who might add to the trust, and all the rest and residue of the undistributed income was to be used by the Board of Trustees for religious, charitable and educational purposes consistent with purposes of the trust, as directed by the Board of Trustees. The trust indenture provided that the vacancies on the Board of Trustees of the trust should be filled as determined by the Elders Body of the Church of the Brethren of the District of Southern California and Arizona [Tr. 84-97].

Included in the properties transferred to the trust was the Davenport residence or home place at 674 Elliott Drive, Pasadena, California [Tr. 52]. It was later agreed by the Board of Trustees and the trustor that the Davenport home place had been transferred in trust by mistake and had not been intended to be a part of the initial trust [Tr. 53]. Accordingly, on or about March 26, 1940, the trustee reconveyed this property to the trustor, Levi M. Davenport [Tr. 53, 75, 113, 114].

Included in the properties conveyed to the trust was a parcel of real property known as the "First Street Property." After the trust had been created, the trustor and the Board of Trustees considered it advisable to make certain improvements on the First Street Property [Tr. 54-55]. The trustee was advised by its attorney that it could not borrow money for the benefit of the trust, but that it would be possible to convey the property back to the trustor, have him borrow the money, make the im-

provements and convey it back to the trust again [Tr. 55]. This plan was followed, the reconveyance to the trustor was made, the property was improved, and then conveyed to petitioner which had been incorporated in the meantime to take over the properties formerly held in the trust [Tr. 74, 110 to 113, incl.].

When the trust was created, it was not contemplated that the trust properties would be turned over to a special corporation until the death of the trustor [Tr. 96]. However, Levi M. Davenport was dissatisfied with the trust arrangement for two reasons—(1) he had been informed that the trustee could not borrow money to improve properties and (2) he had created the trust before he quite worked out his plans for arranging some little security for his daughter, other children and brother. He did not like the arrangement in the trust indenture whereby, within the discretion of the trustees, amounts could be paid to his brother and children in case of their want. Accordingly, the corporation was formed during the life of Levi M. Davenport to cure the undesirable features of the trust [Tr. 53 to 58, incl.].

Shortly after petitioner was formed, namely, on October 8, 1940, LaVerne College, as trustee, transferred to petitioner all the real and personal property which it then held under and by virtue of the trust created by Levi M. Davenport and Barbara N. Davenport, his wife [Tr. 75, 135 to 138, incl.].

On or about May 31, 1941, Levi M. Davenport and his wife transferred to petitioner the Davenport "home place" [Tr. 76, 139]. Contemporaneously therewith petitioner and the transferors executed an annuity agreement whereby (a) the transferors retained the right to use the home place for their lives, (b) petitioner agreed to pay

Lucile Davenport Weller, transferor's daughter, an annuity of \$100.00 per month and upon her death, to pay to her daughter, Dorothy May Weller, a conditional annuity of \$100.00 per month. Petitioner's obligation to pay such annuities was absolute and not dependent upon whether petitioner had net income or net earnings. The annuity to Dorothy May Weller was to be reduced under certain conditions not now material [Tr. 131 to 148, incl.]. Levi M. Davenport and his wife continued to live in the home place throughout the remainder of their lives, petitioner paying the taxes and other expenses of upkeep of its property [Tr. 77, 78]. Barbara N. Davenport died in November, 1943, intestate [Tr. 60, 68]. Levi M. Davenport died January 6, 1947, intestate [Tr. 81].

On or about May 31, 1941 Levi M. Davenport and his wife transferred to petitioner the aforementioned First Street property subject to a reservation whereby Levi M. Davenport received the net income from such property for his life and subject to an exception from the transfer of the right to designate in writing during his lifetime the disposition of such net income for a period not to exceed ten years after his death [Tr. 139 to 142, incl.]. Levi M. Davenport thereafter received directly the rent from such property and paid the taxes thereon [Tr. 77]. Petitioner paid certain expenses of upkeep as follows:

1940	\$ 8.62
1942	63.02
1943	350.70
1944	1,297.78

If and to the extent that Levi M. Davenport should have paid such expenses, petitioner will offset such amounts against moneys owing him [Tr. 63].

The right of Levi M. Davenport to receive the net income of the "First Street Property" for life was in lieu of, and cut off, his right set out in the original trust indenture to receive \$400.00 per month for life [Tr. 55, 58, 63, 64, 65].

Levi M. Davenport considered and intended that the arrangements made on May 31, 1941, for his daughter, Lucile M. Davenport, in the form of \$100.00 annuity and the reservation by him of the right to designate the income from the "First Street Property" for ten years after his death, was to be in lieu of and a substitute for the provisions in the trust indenture whereby the trustees might, in their discretion, pay amounts to the brother and children of Levi M. Davenport in case any of them might "come to want" [Tr. 55 to 59, incl.]. Many years prior to the creation of the trust Levi M. Davenport had given \$35,000.00 to each of his two sons and they had proceeded to create some property values and income for themselves and had such a financial standing that they were not likely to be in need of help from their father or his trust or petitioner. Levi M. Davenport had given his daughter, Lucile Davenport Weller, much less than \$35,000.00 and hence the provision in the trust indenture that the trustees could in their discretion give something to his children in case of want. It was his daughter he was particularly concerned about [Tr. 53]. In forming the corporation he wished to make more definite arrangements for his brother and to cut off or terminate the indefinite arrangements set out in the trust indenture [Tr. 58]. Accordingly, he made the provision of a \$100.00 annuity for his daughter and kept it within his power to arrange for his brother and other children if necessary or desirable by virtue of his right to designate the income from the "First



Street Property” for ten years after his death. However, Levi M. Davenport did not during his lifetime make any such designation of the “First Street Property” to take effect after his death [Tr. 58, 60, 69, 70]. His brother, as well as his sons and daughter, had adequate financial resources of their own [Tr. 67 to 71, incl.].

In 1940 petitioner paid \$1,000.00 to Lucile Davenport Weller, daughter of the donor, and in 1941 paid \$625.00 to Homer Davenport, the son of the donor, in satisfaction of their claims against the assets which the donor transferred to petitioner and its predecessor [Tr. 78]. Practically all of the assets which went into petitioner and its predecessor had been in a corporation called L. M. Davenport Company. Lucile Weller had stock of a par value of \$1,000.00 in such company and Homer Davenport had stock of a par value of \$625.00 in such company. The L. M. Davenport Company was dissolved and the assets deeded to Levi M. Davenport, subject, however, to the claims of the two minor stockholders. Levi M. Davenport deeded the property to the trustee subject to such claims and the trustee deeded it to petitioner subject to such claims and eventually the claims were paid by petitioner [Tr. 66-70, incl.].

Neither petitioner’s Articles of Incorporation nor By-Laws authorize it to distribute income to private individuals [Tr. 118, 124 to 134, incl.], although it is authorized to accept property subject to such conditions and limitations as may be imposed by the donor in connection with property so acquired [Tr. 115, 133].

During the years involved petitioner made contributions to religious, charitable or educational organizations exempt from Federal income tax under Section 101(6) of the Internal Revenue Code, in amounts aggregating \$20,-

124.09. This included the organizations listed on page 79 of the transcript, total \$19,881.09 and those listed in items 3, 4 and 6 on page 80 of the transcript, total \$243.00 [Tr. 63, 64, 65, 72]. (The 1943 contribution to Radio Gospel Hour was \$50.00 instead of \$5.00, as shown on page 80.) During the same years it made contributions to religious, educational and charitable organizations for which no known exemption from income tax has been granted, as follows [Tr. 71 80]:

	1941	1942	1943	1944
United American De- fense Committee	\$25.00			
National Voice		\$15.00	\$15.00	\$35.00
W. M. Miles Radio Program				10.00
State-Wide Committee, Higher Education				2.00
Los Angeles Times		24.50		
	<hr/> \$25.00	<hr/> \$39.50	<hr/> \$15.00	<hr/> \$47.00
	<hr/>	<hr/>	<hr/>	<hr/>
Total				\$126.50

In each of the years under review petitioner paid \$10.00 to the Property Owners Association of Los Angeles, California, an organization exempt under Section 101(8) of the Internal Revenue Code. That organization assists taxpayers in keeping down the local taxes and petitioner made the contribution to that organization for the purpose

of trying to keep down the taxes on its property [Tr. 64, 81].

Levi M. Davenport, as founder of petitioner, generally directed its affairs during his lifetime. He caused petitioner to make contributions to organizations which were not exempt under Section 101(6) of the Internal Revenue Code as follows [Tr. 80]:

	1940	1941	1944
Democratic Club for Wilkie, Los Angeles	\$14.18		
Jeffersonian Democrats, Los Angeles	10.00	\$25.00	
Republic Club, Los Angeles, Cal.			\$25.00
Democrat Club, Los Angeles, Cal.			25.00
	<hr/>	<hr/>	<hr/>
	\$24.18	\$25.00	\$50.00
	<hr/>	<hr/>	<hr/>
Total			\$99.18

Petitioner intends to charge Levi M. Davenport for such unauthorized contributions by withholding amounts owing to him [Tr. 63].

The only other amounts paid out by petitioner during the years involved were for business expenses which have been allowed as deductions by the respondent [Tr. 150].

### Specification of Errors Relied Upon.

1. The Tax Court erred in failing to find that the provisions made for the grantor and his family amounted to reservations and exceptions from the properties transferred to petitioner and its predecessor.

2. The Tax Court erred in failing to find that some of the provisions of the predecessor trust made for members of the grantor's family were discretionary provisions and were cut off when petitioner was organized.

3. The Tax Court erred in failing to find that in any event the members of petitioner's family were in such financial condition that they did not and were not likely to, call upon petitioner for financial assistance.

4. The Tax Court erred in failing to find that if petitioner, under the management of the grantor, made any improper payments, petitioner will recoup such payments from the grantor by withholding moneys due him or by claims against his estate.

5. The Tax Court erred in failing to find that payments made by petitioner to two of grantor's children were in discharge of claims held by such children against the petitioner's assets.

6. The Tax Court erred in failing to find that certain payments to several organizations were for religious, educational and charitable work or were business expenses of petitioner.

7. The Tax Court erred in failing to find that petitioner was exempt from income and declared value excess



profits tax for the years 1940 to 1945, inclusive, under the provisions of Sections 101(6), 600, 1200 and 1201(a)-(1) of the Internal Revenue Code.

8. The Tax Court erred in holding that petitioner distributed some of its income to organizations or persons not exempt from tax.

9. The Tax Court erred in holding that petitioner was not exempt because it did not distribute, during the taxable years, the entire amount of its income.

10. The Tax Court erred in failing to find that petitioner was exempt from income and declared value excess profits taxes for the years 1940 to 1944, inclusive, under the provisions of Sections 101(14), 600, 1200 and 1201(a)(1) of the Internal Revenue Code.

11. The Tax Court erred in rendering decision for the respondent.

### **Statutes Involved.**

Section 101 of the Internal Revenue Code exempts from income tax certain corporations. The applicable paragraphs read as follows:

Section 101(6) of the Internal Revenue Code reads as follows:

“(6) Corporations, and any community chest fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or

individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation”;

Section 101(14) of the Internal Revenue Code reads as follows:

“(14) Corporations organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof, less expenses, to an organization which itself is exempt from the tax imposed by this chapter”;

### Summary of Argument.

While petitioner received the legal title to all the properties conveyed to it, it did not receive the entire *fee interest* in such properties. It received only the remainder after certain reservations in favor of the grantor and after certain exceptions in favor of members of the grantor's family. *Petitioner's* entire interest in the property, as distinguished from interests reserved for others, was to be, and has been, devoted exclusively to religious, educational and charitable purposes.

The use by the Davenports of the Davenport home, the collection of the income from the “First Street Property” by Levi M. Davenport and the receipt by Lucile Weller of the \$100.00 annuity did not constitute the receipt by them of part of *petitioner's* income, as such items were never a part of petitioner's assets or income but were always properties and rights reserved from property transferred to petitioner.

The provisions in the original trust for payment of \$400.00 per month to Levi M. Davenport out of the income of the trust and a contingent and discretionary payment to his brother and children was cut off and terminated, by other and substitute provisions, when petitioner was incorporated.

The \$1,625.00 paid by petitioner to the donor's children was in satisfaction of claims they had against the assets transferred to petitioner subject to such claims.

Petitioner's income was either accumulated for improvement of the properties or expended for ordinary business expenses or distributed to religious, educational or charitable organizations, most of which had been held exempt from income tax. Very small amounts were paid out for unauthorized expenditures such as contributions to political organizations but these expenditures will be recouped by petitioner by withholding amounts payable to the donor.

Thus petitioner is and was a corporation organized and operated exclusively for religious, charitable and educational purposes, no part of the net earnings of which inured to the benefit of any private individual and no substantial part of the activities of which was carrying on propaganda or otherwise attempting to influence legislation and hence was exempt under Section 101(6) of the Internal Revenue Code.

In the alternative, petitioner was exempt under Section 101(14) of the Internal Revenue Code because it was a corporation organized for the exclusive purpose of holding title to property, collecting income therefrom and turning over the entire amount thereof, less expenses, to organizations which themselves were exempt from the tax imposed by this chapter. The fact that taxpayer accumulated some of its earnings for improvement of its properties does not deprive it of exemption under this paragraph as such income will eventually be used for the statutory purposes. The minor contributions to charitable, religious and educational organizations which apparently have not obtained exemptions from income tax should be ignored under the *de minimis* rule.

Petitioner's own assets and income, exclusive of life estate and other reserved interests, were to be used and were used solely for religious, charitable and educational purposes and no part of petitioner's own assets and income was used or was to be used for payments to Levi M. Davenport or any member of his family.

The authorities are in complete agreement that the reservation by a donor of an interest in property or an annuity does not affect the exemption of a charitable organization which receives a gift. The Tax Court conceded this point but erred in failing to find that all of the amounts which went to individuals were received by them by virtue of reservations and exceptions in the transfers to petitioner.



## ARGUMENT.

### **Petitioner Is Exempt From Tax Under Section 101(6) of the Internal Revenue Code.**

It is admitted by both the respondent and the Tax Court that petitioner was a non-profit California corporation organized to act as trustee under Christian educational, charitable, eleemosynary and other charitable trusts and that it had no provisions for distributing its income to anyone.

It has also been stipulated that most of its income during the years involved was paid out as contributions to religious educational and charitable organizations which were exempt from income tax.

The controversy arises over the fact that with respect to some of the properties to which petitioner held legal title (a) the donor had the right to use one piece and was entitled to receive the income from another, (b) the donor's daughter was entitled to an annuity of \$100.00 per month for her life, with a contingent annuity for the life of her daughter, (c) there is disagreement as to whether some of the income might be used for the donor's brother and children, (d) minor amounts were paid for the upkeep of one of petitioner's properties which possibly should have been paid by the donor, and (e) minor contributions were made to political organizations for which petitioner is entitled to recoupment.

It is the petitioner's position that anything that was used or received or retained by the donor and his family came by way of a reservation or exception from the grant

of property to petitioner, and the receipt by the donor and his family did not constitute a receipt of *petitioner's* income, as such property or income never became petitioner's property or income. This matter will be discussed first and the other points will be taken up thereafter.

**(A) The Reservation, by a Donor of Property to an Otherwise Exempt Corporation, of an Interest in Property or an Annuity Payable to the Donor or Others, Does Not Destroy the Exemption of the Donee.**

The leading case to the effect that the reservation by a donor of an interest in property or an annuity does not affect the exemption of a charitable organization which receives the gift is *Lederer v. Stockton*, 260 U. S. 3. In that case a decedent had devised property to a charitable corporation subject to the payment of certain annuities. The Supreme Court held that the payment of annuities did not destroy the exemption of the charitable corporation and on page 8, the Court said:

“This residuary fund was vested in the Hospital. The death of the annuitant would completely end the trust. For this reason, the trustee was able safely to make the arrangement by which the Hospital has really received the benefit of the income subject to the annuity. As the Hospital is admitted to be a corporation whose income when received is exempt from taxation under Section 11(a), we see no reason why the exemption should not be given effect under the circumstances. To allow the technical formality of the trust, which does not prevent the Hospital from really enjoying the income, would be to defeat the beneficent purpose of Congress.”

One of the clearest statements of the applicable law is set forth in *Emerit E. Baker, Inc. v. Commissioner*, 40

B. T. A. 555, Acq. 1940-1 C. B. 1. There taxpayer was organized in 1924 as a non-profit charitable corporation. Its principal organizer was Emerit E. Baker. The taxpayer operated for charitable purposes under the direction of Emerit E. Baker and six of his associates. In 1929, Emerit E. Baker died, leaving a will appointing the taxpayer as executor and trustee of his residuary estate. The will provided that the taxpayer, as trustee of the residuary estate, should pay decedent's wife an annuity of \$12,000.00 a year, which should be paid out of the trust corpus if the income should be insufficient. The will also provided for the continuance of payments for the education of any pupils in school being maintained by the decedent at the time of his death. It then provided that any additional income be used for certain specific charitable purposes to aid the City of Kewanee, Illinois, the purposes of which were essentially similar to those for which the taxpayer was formed. Decedent's widow, in lieu of asserting her dower right, agreed to accept an annuity from taxpayer of \$19,200.00 per year or \$7,200.00 per year more than was provided in the will. The Commissioner assessed deficiencies against taxpayer on the basis that it was not an exempt corporation because of the annuity paid to decedent's widow and other payments made for the educational expenses of certain of the widow's nieces and nephews who were being helped by decedent at his death.

The Board of Tax Appeals held that the taxpayer was an exempt corporation by reason of its charitable nature. With respect to the Commissioner's contentions regarding the annuity and other payments, the Board at page 561 said:

"Petitioner's only activity during the taxable years which was not strictly of a charitable or educational

character was the payment of the allowance to the decedent's widow and the educational expenses of her nieces and nephews. We do not think that that alone defeats its classification as an exempt corporation under the statute. The payment of these amounts was merely incidental to and was a means of furthering the charitable and educational purposes for which the petitioner was organized. It was in no sense a part of its corporate activities. The payments made to the widow and nieces and nephews were a charge not upon the petitioner's net earnings but against the entire corpus of the residuary estate."

In *Estate of J. B. Whitehead v. Commissioner*, 3 Tax Ct. 40, affirmed 147 F. (2d) 977, the same rule was announced. In that case the decedent left his entire estate subject to certain special bequests to a charitable foundation to be formed after his death. The will provided that certain settlement contracts with a former wife and his wife at the time of death, be carried out, and also provided for the payment of two annuities of \$5,000.00 and \$7,500.00 per year, respectively, to two individuals. The taxpayer in that case paid the widow \$500,000.00 in settlement of her claim for the entire estate. The Commissioner refused to allow the decedent's estate to deduct from the gross estate the amounts paid to the charitable foundation, on the ground that the charitable foundation did not qualify as an exempt corporation. The Tax Court in holding that the corporation was a charitable one and that the payments were deductible, said:

"To hold that discharge of such claims against an estate as those of the widow, and the former wife, based upon law or contracts and payable in any event, destroys a broad testamentary provision that the *residuum* of the estate go to charity would, no doubt,



tend to strike down very many testamentary charities, for it can hardly be thought that an estate would have no claims against it at all."

The United States Circuit Court of Appeals for the Fifth Circuit, in affirming the Tax Court's decision, said:

"We find it sufficient to say that the terms of the will, the facts surrounding its execution and administration, and the condition of the estate at testator's death, leave us in no doubt that his purpose to create a charitable trust, to devise to it, subject only to the payment of its known debts for which he had ample cash on hand, all of his property, and, subject to the payment out of it of certain small bequests, to dedicate and devote the entire income therefrom to charitable uses, has been sufficiently indicated and must be given effect."

To the same effect, see *Pasadena Methodist Foundation v. Commissioner*, Tax Ct. Memorandum Decision, Docket No. 109667 and 109668, entered October 11, 1943, C. C. H. Decision 13, 544M; *Home Oil Mill, et al v. Willingham*, 68 Fed. Sup. 525, appealed by government, dismissed on government's motion January 9, 1947, Prentice-Hall Fed. Tax Service, paragraph 72304. See also I. T. 1776, C. B. II-2, 151; I. T. 3707, C. B. 1945, 114; I. T. 2397, C. B. VII-1, 90; and G. C. M. 3016, C. B. VII-1, 90.

Petitioner's claim for exemption in the present case is supported by several rulings of the Bureau of Internal Revenue. Thus, in I. T. 1776, C. B. II-2, 151, it was

held, under the Revenue Act of 1921, that where a donor gave a life estate in bonds to an individual and the remainder interest to a church, the cash value of the gift to the church was deductible. In I. T. 3707, C. B. 1945, 114, it was held that where a taxpayer creates an irrevocable trust, reserving the income to himself for life with remainder over at his death to a beneficiary which meets the requirements of Section 23(o)(2) of the Internal Revenue Code, the present value of the remainder interest is deductible as a charitable contribution. In I. T. 2397, C. B. VII-1, 90, it was held that where taxpayer transferred \$50,000.00 to a college upon an agreement that he should receive an annuity of \$2,500.00 per annum, the difference between the \$50,000.00 and the present value of the annuity was deductible as a charitable contribution under Section 214(a)(10) of the Revenue Act of 1926. In G. C. M. 3016, C. B. VII-1, 90, it was held that where, upon the death of the survivor of two life beneficiaries, the principal of a trust fund was to be paid to an agency organized and operated exclusively for charitable, scientific or educational purposes, the present value of the remainder interest was deductible under Section 214(a)(10) of the Revenue Act of 1926.

Since reservations by donor to an otherwise exempt corporation did not destroy its exemptions, there remains the problem of determining which of the payments to the donor or his family in the instant case were required by reservations.

**(B) All the Payments to Be Made by Petitioner to Donor and His Family Were Required by Reservations and Exceptions From the Properties Contributed to Petitioner by Donor.**

When Levi M. Davenport transferred properties to the trustee he transferred them with the following reservations for himself; (1) \$400.00 per month during the term of his natural life; (2) the right to live in the Davenport home, rent free, during his life.

He also made an exception from the property transferred to the trustee in the form of a provision for his brother and children should they "come to want," at the discretion of the Board of Trustees.

The Davenport home and the "First Street Property" were conveyed by the trustees back to Levi M. Davenport and were in his hands at the time petitioner was created. Petitioner received the remainder of the property in the trust subject to the terms of the trust.

On May 31, 1941, Levi M. Davenport transferred the Davenport home and the "First Street Property" to petitioner in such manner as to affect and change all the reservations and exceptions upon which the property had originally been transferred to the trust.

With respect to the Davenport home, he reserved the right for the life of himself and his wife, Barbara N. Davenport, to live in the home. At the same time he excepted from the grant of the Davenport home to the petitioner, an annuity of \$100.00 per month payable to his daughter and upon her death a conditional annuity of \$100.00 or \$50.00 per month payable to her daughter. This latter provision satisfied Levi M. Davenport that his daughter would have some security and he intended that this provision would terminate the provision in the trust

whereby the trustees might, at their discretion, pay something to his daughter in case of her want.

Also on May 31, 1941, Levi M. Davenport deeded the "First Street Property" to the petitioner but reserved for himself the right to receive the net income from this property for his lifetime. This provision was intended to and did terminate his right to receive \$400.00 per month, provided for in the original trust indenture. He also excepted from said deed to the petitioner the right to designate in writing, during his lifetime, the disposition or use of said net income for a period not to exceed ten years after his death. This latter provision was intended by Levi M. Davenport to be in lieu of and to terminate the right and power of the trustees, in their discretion, to give some of the trust income to petitioner's other children or brother in case of their want.

Consequently, all of the rights remaining in or going to the grantor and his family were created by reservations or exceptions from the deeds of property to petitioner or its predecessor. As a matter of law, therefore, none of those rights ever belonged to petitioner, *Blair v. Commissioner*, 300 U. S. 5; *Estate of Homer Laughlin*, 8 T. C. 33. Petitioner received the balance only of the interests in the properties deeded to it. The grantor reserved some of those interests for himself and excepted from the deeds interests in favor of others. These interests reserved and excepted were, therefore, excluded from the operation of the deeds or grants and were never in petitioner. Consequently, when petitioner allowed the grantor to use the home or to receive the income from the "First Street Property" and when petitioner paid the annuity to grantor's daughter, it was not paying out its own income or money but simply turning over to those persons their



own property or money which never was the property of petitioner.

The respondent argues that the provision in the original trust indenture whereby the brother and children of the donor might, in the discretion of the trustees, receive some of its income in case of their want, has not been cut off by the agreements of May 31, 1941 and are so indefinite and uncertain that they might take up all of the net income of petitioner and hence the petitioner was primarily organized for private and not for charitable purposes.

The testimony showed that it was the belief and intention of the grantor that the annuity provided for the daughter, and the right in the grantor to dispose of the income of the "First Street Property" for ten years after his death, were to take care of his brother and children and were to cut off the previous rights in their behalf. The testimony also showed that the brother and children were in good financial condition and were not likely to call upon the petitioner for help. Furthermore, the directors of petitioner would naturally assume that the terms of the original trust whereby they might pay something to the brother and children of the grantor had been changed by the May 31, 1941 documents since that was the intention of the grantor and the interpretation he put upon them.

Finally, if the provisions of the original trust still remain in effect after May 31, 1941, and if they are so uncertain and indefinite as indicated by the respondent, then such uncertainty renders the exceptions void. Uncertainty which renders exceptions void accrues to the benefit of the grantee and does not invalidate the entire grant but merely leaves it free and clear of the exceptions. See 26 Corpus Juris Secundum, page 457. Therefore, under the respond-

ent's own argument, petitioner is free of any requirement to distribute money to the grantor's brother or children.

The Tax Court has recognized that the reservation by the grantor of the right to use the Davenport home and the right to the income of the "First Street Property" was a reservation and does not deprive the petitioner of its exemption. The Tax Court on this point said:

"If the 'First Street Property' and the home property which were transferred to the petitioner, subject to reservations, were the only properties here involved, similarity of the cases might prevent their distinguishment." [Tr. 41.]

Petitioner submits that the use of the Davenport home and the use of the income from the "First Street Property" were reserved by the donor and such interests never belonged to the petitioner and hence were never paid out by Petitioner from its property or income to private persons.

The same is true with respect to the annuity to the daughter. This was an exception from the grant to petitioner and the \$100.00 per month never was petitioner's property or income and hence when petitioner paid it out to the grantor's daughter, such act did not amount to a distribution of petitioner's income to private parties and hence does not destroy petitioner's exemption.

With respect to the provisions for the brother and children of grantor, it is petitioner's position that (1) the provisions in the trust indenture were cut off by the documents and transfers of May 31, 1941, (2) if the trust provisions were not so cut off they are immaterial, as the children and brother will never need to call upon petitioner, (3) if the brother or children do call upon petitioner,

petitioner will consider that their rights were cut off as was intended by the grantor and will exercise its discretion to deny their request, (4) even if the rights still subsist and if payments are made to the brother or children, they will have been made by virtue of exceptions made by the grantor when he transferred the property to petitioner and its predecessor. Hence, the amounts disbursed to the brother and children would not be disbursements of petitioner's property or money but disbursements of property or money reserved or accepted from the grant and never belonging to petitioner.

This brings us now to the final item which was paid to members of petitioner's family, namely, the \$1,000.00 to the daughter and the \$625.00 to the son. Here again, these amounts were not petitioner's property or money paid out but were the property of the claimants.

The donor, Levi M. Davenport, owned most of the stock of the L. M. Davenport Company. His daughter and son had stock interests of \$1,000.00 and \$625.00, respectively, therein. That company was dissolved and its assets deeded to Levi M. Davenport, but he took the property for himself and as trustee for the other stockholders who had claims against such property and were owners of portions thereof. Levi M. Davenport then deeded the property to the trustee, but, of course, deeded it subject to liens, encumbrances, or trusts outstanding against it. Petitioner took only such interest as the grantor had and took it subject to the condition of the title. Eventually the petitioner paid the daughter and the son the \$1,000.00 and the \$625.00, respectively, for their interests in the property and their claims against it.

Here, again, petitioner was merely turning over to other people, their property which had been placed in petitioner's

hands. This does not amount to a distribution of petitioner's property or petitioner's income to private persons, as it never was petitioner's money or income.

Hence, any rights or moneys which donor or his family received or might receive from petitioner were required by reservations and exceptions from the deeds transferring the property to petitioner and were not distributions of petitioner's money or income and do not deprive petitioner of exemption.

By the time this case was tried in the Tax Court, Levi M. Davenport and his wife, Barbara N. Davenport, had both died. Levi M. Davenport had not appointed the income of the "First Street Property" for any period after his death. As a consequence, out of the \$270,000.00 worth of property which they transferred to petitioner and its predecessor the following is all that the grantor and his family received or will ever receive:

1. The use of the Davenport home for about  $7\frac{1}{2}$  years (May 23, 1939 to January 6, 1947),
2. The income from the "First Street Property" for about  $5\frac{1}{2}$  years (May 31, 1941 to January 6, 1947),
3. An annuity of \$100.00 per month from May 31, 1941, for the daughter who was born on May 20, 1893, and hence was 53 years old at the time of the trial, and a conditional annuity for a younger woman who probably will never take anything under it.

The rental value of the home was \$1,500.00 per year, making the total for  $7\frac{1}{2}$  years \$11,250.00, and the net income of the "First Street Property" was \$4,800.00 per year, a total of \$26,400.00 for the  $5\frac{1}{2}$  years. The reservations of these up to the date of the trial amounted in



value to but \$37,650.00, a small portion of the value of the property granted to petitioner. The annuity of \$1,200.00 per year to the daughter is equal to but a small fraction of the net income of petitioner, which averaged, before any contributions were made to charity, something over \$9,000.00 per year. The total amount the daughter would receive from May 31, 1941, until the end of her life expectancy would be about \$26,000.00.

Thus the total amount paid or likely to be paid to the grantor and his family would hardly exceed \$63,650.00, leaving to petitioner at least \$206,000.00 and the income therefrom for religious, charitable and educational work.

It would scarcely seem, therefore, that the petitioner was organized more for private than for charitable purposes. Grantor gave at least three-fourths of all his property for charitable, religious and educational purposes and retained only one-fourth for himself and family.

The grantor's action was certainly charitable and it is prayed that minor informalities or defects in the beneficent plan be judged with equal charity.

**(C) All of Petitioner's Authorized Contributions Were Made for Charitable, Religious and Educational Work.**

As seen by the provisions of the trust indenture, the grantor obviously believed in extending education in religious matters. He provided that the trustees should pay to the LaVerne College \$3,600.00 per year for the purpose of establishing a Department of Philosophy and Religion. He also provided that the trustees could, in their discretion, pay \$300.00 per year to the American Bible Society and such other amounts for similar purposes as the trustees should decide upon.

Levi M. Davenport, as the creator of the trust and the donor of the property to petitioner, was the dominant power in the operation of petitioner throughout his life. His deeply religious nature led him to cause petitioner to make contributions for various educational, religious and charitable purposes. On page 79 of the Transcript is shown the contributions made by petitioner during the years involved. They include amounts to the LaVerne College, Los Angeles Tuberculosis & Health Association, the various War Chests, American Red Cross, Children's Home Society, American Bible Society, United China Relief, Boys Clubs, American Mission to Lepers, Church of the Brethren and various religious radio programs. All of the institutions shown on page 79 and those listed as items 3, 4 and 6 on page 80 of the Transcript, were organizations which had obtained exemption from income tax because of their charitable, religious and educational work. The bulk of petitioner's net income went to such organizations. Some of its income it retained for improvement and enlargement of its properties, which resulted in an increase in its income. See Transcript 149 and 150.

In addition to the contributions to organizations for which tax-exemption certificates had been granted, petitioner also made similar contributions to other religious, educational and charitable organizations for which no known exemption from income tax has been granted. These were as follows:

United American Defense Committee.

National Voice.

W. N. Miles Radio Program.

State Wide Committee, Higher Education.

The Los Angeles Times.

All of these organizations carried on work of a religious, charitable or educational nature. As to the National Voice, testimony showed that its work was religious education. In any event, it is clear that the work of all was of a religious, charitable and educational nature, of a type which petitioner was permitted to assist and still be exempt from income tax.

**(D) Petitioner Is to Be Repaid for Any Expenditures Made for Unauthorized Purposes.**

Levi M. Davenport was an aged man, born August 4, 1861. He was 78 years of age when the trust was created. Being the sole contributor of the trust, it was natural that he would dominate its benefactions. Not being tax minded, it was natural that the trust would be run with informality and that he might make some contributions to organizations which did not technically qualify under Section 101(6) or 101(14) of the Internal Revenue Code.

Mr. Davenport caused petitioner to make contributions to Republican and Democratic Clubs during the 1940 and 1944 national campaigns in a total amount under \$100.00. Since he contributed to both parties it would appear that his purpose was more educational than political.

Under the original trust indenture Levi M. Davenport was to receive \$400.00 per month for life. Under the agreement of May 31, 1941, he was to receive the net income of the "First Street Property" for his life. The rental value of this property was \$5,400.00 per year and the taxes amounted to about \$600.00 per year, leaving a net of \$4,800.00 per year. Levi M. Davenport considered that the net income from the "First Street Property" was equal to the \$400.00 per month he was to receive under

the original trust indenture and he took the second provision in place of the first. After May 31, 1941, he never requested or received the \$400.00 per month provided for in the original trust agreement.

Levi M. Davenport directly collected from the tenant the rent from the "First Street Property" and paid the taxes thereon. He considered that this was all he was required to do. Petitioner paid other upkeep expenses of the property aggregating in the taxable years \$1,720.12. The grantor interpreted the term "net income" as meaning the gross rent less the taxes. If another interpretation of the term "net income" would have required him to pay the upkeep of the property, then he has caused petitioner to pay out money which it should not have paid, for his benefit. If that is the final interpretation of the directors, they have testified that they would withhold from moneys owing him, the amount of such unauthorized expenditures so caused to be made by petitioner.

The Tax Court seems to think [Tr. 42], that the petitioner should not have paid the taxes and maintenance expenses on the Davenport home while it was occupied by Levi M. Davenport. Petitioner does not agree with this interpretation as, under the agreement of May 31, 1941 [Tr. 139-141], donor and his wife transferred the home property to the petitioner "subject to the right of the donors and the survivor of them to the use thereof for and during the term of their and each of their natural lives." Since the remainder interest in the property belonged to petitioner, naturally it had to pay the taxes and upkeep in order to protect its interests. The donor and his wife were entitled to the use of the house, rent free, with expenses paid by petitioner. It is believed that petitioner was required by the terms of the contract to pay



the taxes and upkeep expenses and that the payment thereof by petitioner did not constitute a distribution of petitioner's income to the donor or his wife. If Levi M. Davenport was supposed to pay such taxes and upkeep on the home, then petitioner will recoup itself out of moneys owing to him or out of his estate.

## II.

**In the Alternative Petitioner Was a Corporation Organized for the Exclusive Purpose of Holding Title to Property, Collecting Income Therefrom and Turning Over the Entire Amount Thereof, Less Expenses, to an Organization Which Itself Is Exempt From Income Tax.**

If the Court holds that petitioner was not exempt from income tax under the provisions of Section 101(6) of the Internal Revenue Code, then it is submitted that petitioner is exempt from tax under the provisions of Section 101(14) of the Internal Revenue Code.

After excluding from consideration payments required to be made by petitioner by virtue of reservations and exceptions in the deeds and grants from the donor to petitioner of various parcels of property, all of petitioner's authorized contributions were made to organizations exempt from income tax. In G. C. M. 11,817, C. B., June, 1933, page 56, the respondent conceded that the right to exemption from Federal income tax under Section 101-(14) of the Internal Revenue Code is not defeated where a holding corporation pays its income to several organizations, each of which is entitled to exemption.

As shown heretofore in this brief, all of the rights and benefits which the grantor and his family received or retained were reserved to them or retained as exceptions

in the deeds and transfers made to petitioner. Hence, those rights and benefits were never petitioner's property or income and hence were not distributed by petitioner to such private persons. Only the excess over and above the amounts reserved or excepted from the deeds, were petitioner's property and that is all for which petitioner needs to account.

The contributions which petitioner made from its own property and income were made to organizations exempt from income tax. This point has been discussed in a preceding portion.

Petitioner did make a few contributions to charitable, religious and educational organizations for which no known exemption from income tax has been granted. It paid out during the years involved \$20,124.09 to organizations for which exemption had been granted and \$126.50 to religious, educational and charitable organizations for which no known income tax exemption has been granted.

The \$126.50 paid to religious, charitable and educational organizations for which no known income tax exemption has been granted, should be ignored under the doctrine of *de minimis*. Those organizations probably can secure exemption or may even have it but petitioner was unable to determine whether or not exemption had been granted to them. The amount involved is so small as compared with the total benefactions that they should not be allowed to deprive petitioner of its exemption.

The amounts paid each year to the Property Owners Association of Los Angeles, California do not tend to deprive petitioner of exemption as the Property Owners Association was exempt from income tax under the pro-

visions of Section 101(8) of the Internal Revenue Code. It, therefore, qualifies under Section 101(14).

Here, again, if petitioner made any unauthorized distributions, whether to political clubs or on property the maintenance of which might have been payable by the donor, this will not tend to deprive petitioner of exemption, as it is entitled to and will receive recoupment from the donor for these expenditures.

The fact that petitioner might have accumulated some of its income for the enlargement or improvement of its properties does not deprive it from exemption under Section 101(14) of the Code, as all of its income must eventually be turned over to tax exempt organizations and that is all that the statute requires. It does not require that it turn it over currently or annually, but only eventually.

### III.

#### **Petitioner Is Exempt From Declared Value Excess Profits Tax.**

Petitioner has shown that it is exempt from Federal income tax under either Section 101(6) of the Internal Revenue Code or Section 101(14) thereof. Section 600 of the Code imposes a declared value excess profits tax on corporations subject to capital stock tax under Section 1200 of the Code. Section 1201(a)(1) of the Code provides that the capital stock tax imposed by Section 1200 shall not apply to corporations enumerated in Section 101 of the Code. Accordingly, petitioner is exempt from declared value excess profits tax.

**Summary.**

On the basis of the law and the facts, it is submitted that petitioner is exempt from Federal income tax under Section 101(6) of the Internal Revenue Code or under Section 101(14) of the Code; and that petitioner is exempt from declared value excess profits tax under Sections 600, 1200, 1201(a)(1) of the Code.

Respectfully submitted,

MELVIN D. WILSON,

*Counsel for Petitioner.*



No. 11912

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**In the United States Circuit Court of Appeals  
for the Ninth Circuit**

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**THE DAVENPORT FOUNDATION, PETITIONER**

*v.*

**COMMISSIONER OF INTERNAL REVENUE, RESPONDENT**

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**ON PETITION FOR REVIEW OF THE DECISION OF THE TAX  
COURT OF THE UNITED STATES**

---

**BRIEF FOR THE RESPONDENT**

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# INDEX

	Page
Opinion below.....	1
Jurisdiction.....	1
Question presented.....	2
Statute and regulations involved.....	2
Statement.....	2
Summary of argument.....	8
Argument:	
I. The purposes for which the Foundation existed and the use of its funds denied it exemption under Section 101 (6) of the Internal Revenue Code.....	9
II. The Foundation was not organized exclusively to hold title to property, collect income therefrom and turn over the entire amount less expenses to an exempt organization and is therefore not exempt under Section 101 (14) of the Internal Revenue Code.....	19
Conclusion.....	22
Appendix.....	23

## CITATIONS

Cases:	
<i>Baker, Emerit E. Inc. v. Commissioner</i> , 40 B. T. A. 555.....	18
<i>Banner Building Co. v. Commissioner</i> , 46 B. T. A. 857.....	20
<i>Home Oil Mill v. Willingham</i> , 68 F. Supp. 525.....	18
<i>Lederer v. Stockton</i> , 260 U. S. 3.....	18
<i>N. P. E. F. Corp. v. Commissioner</i> , decided April 29, 1946.....	21
<i>Pasadena Methodist Foundation v. Commissioner</i> , decided October 11, 1943.....	18
<i>Scholarship Endowment Foundation v. Nicholas</i> , 106 F. 2d 552, certiorari denied, 308 U. S. 623.....	13
<i>Sprunt, James, Benevolent Trust v. Commissioner</i> , 20 B. T. A. 19..	13
<i>Whitehead, Estate of, v. Commissioner</i> , 3 T. C. 40, affirmed <i>sub nom. Commissioner v. Citizens &amp; So. Nat. Bank</i> , 147 F. 2d 977..	18
Statute:	
Internal Revenue Code, Sec. 101 (26 U. S. C. 1946 ed., Sec. 101) ..	23
Miscellaneous:	
Treasury Regulations 103:	
Sec. 19.101-1.....	23
Sec. 19.101 (6)-1.....	24
Treasury Regulations 111:	
Sec. 29.101-1.....	25
Sec. 29.101 (6)-1.....	25
Sec. 29.101-2.....	25





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---

## **BRIEF FOR THE RESPONDENT**

---

### **OPINION BELOW**

The memorandum findings of fact and opinion of the Tax Court (R. 28-43) are not reported.

### **JURISDICTION**

This petition for review (R. 44-51) involves Federal income and declared value excess profits taxes for the calendar years 1940 through 1944. On March 1, 1946, the Commissioner of Internal Revenue mailed to the taxpayer notice of deficiencies in the total amount of \$10,047.83. (R. 7-21.) Within ninety days thereafter and on April 1, 1946, the taxpayer filed a petition with the Tax Court of the United States for a redetermination of that deficiency under the provisions of Section 272 of the Internal Revenue Code. (R. 4-

21.) An amended petition was filed on February 14, 1947. (R. 23-26.) The decision of the Tax Court sustaining the deficiencies was entered December 29, 1947. (R. 43.) The case is brought to this Court by a petition for review filed March 24, 1948 (R. 44-52), pursuant to the provisions of Section 1141 (a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948.

#### QUESTION PRESENTED

Whether or not the Foundation was exempt from taxation under Section 101 (6) or Section 101 (14) of the Internal Revenue Code for the years 1940 through 1944.

#### STATUTE AND REGULATIONS INVOLVED

The statute and regulations involved in this case are found in the Appendix, *infra*.

#### STATEMENT

The facts found\* by the Tax Court (R. 28-37) may be summarized as follows:

The Taxpayer Foundation, hereinafter referred to as the Foundation, the principal office of which is in Pasadena, California (R. 28), was incorporated on July 8, 1940, under the laws of California as a non-profit corporation (R. 33). It is the successor to the Davenport Foundation, a trust (R. 29), hereinafter referred to as the trust, and was created to replace a college as trustee under a trust created by one Levi M. Davenport (R. 33). The stated purpose, in the Foun-

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\*Any reference to the evidence is made by specific record citation other than pp. 28-37.

dation's document of creation, was "To act as Trustee under Christian Educational, Charitable, Eleemosynary, and other charitable trusts" and its charter contains the usual powers and customary provisions found in corporate charters of this character. No provision was made for the distribution of income. (R. 33.)

On May 23, 1939, Levi M. Davenport executed an irrevocable transfer in trust of certain real and personal property to La Verne College as trustee and five persons, including Mrs. Lucile Davenport Weller, the trustor's daughter (R. 66), constituting a board of directors. On the date of the transfer the property had a value of \$261,884. On June 1, 1939, Barbara N. Davenport, the trustor's wife, transferred to the trust two parcels of real estate having a value of \$8,500. (R. 29.)

The trust indenture, under which the transfers were made to the trust, stated that the only duty or obligation of the trustee shall be to hold title to the property and perform such acts as shall be necessary to carry out the orders and directions of the board of directors. The board had complete control, management and operation of the property forming the trust estate and was to collect principal and income and after the payment of specified deductions, to pay, accumulate, use and invest, hold and distribute, funds for the purposes stated in the indenture. No specific purposes were stated but specifications were made under various headings in the indenture (R. 85-96), one of which headings was "Distribution of Income" (R. 29-30).

Under that heading it was provided in Section 1 that \$400 per month was to be paid to Levi M. Davenport, the trustor, for and during the term of his natural life and in Section 3 that suitable and proper provision was to be made for the support and maintenance of the trustor's brother, as his needs might require, not to exceed \$100 per month, and that the board of trustees, solely within its discretion, should use a portion of the income to care for any of the trustor's children as their needs might require, should any of them come to want. Section 5 provided for the payment of annuities to annuitants who added to the trust. In Sections 2 and 4, respectively, it was provided that \$300 per month was to be paid to La Verne College to establish a department of Philosophy and Religion and \$300 per annum to the American Bible Society. (R. 30-31.)

Under the heading "Reservations" the indenture provided that the trustor, Levi M. Davenport, during his lifetime, should have the right to the use and occupation, rent-free, of his residence property or some other home of similar rental value (R. 31-32), and no other specific reservation was made (R. 92).

The indenture provided further that the board of trustees might advise or consult with the trustor regarding the sale or retention of trust property and investment of the trust's funds, or the exercise of any of its powers, and that in following in whole or in part any of his requests or recommendations the board should be free of any responsibility for losses or liability to the trust estate. (R. 95-96.) It provided also



that the trust could not be revoked nor any of the corpus of the trust estate be withdrawn. (R. 96.)

Under "Powers of Trustees" (R. 93, 96), the indenture authorized the board of trustees, after the death of the trustor and the individual beneficiaries, to incorporate the trust "in which event La Verne College shall convey all of its title in the trust estate to such corporation upon request of the board" (R. 32).

Included in the real estate conveyed to the trust by Levi M. Davenport was a parcel known as the "First Street property". After the trust was created the trustor desired to improve that property and when the trustee was advised that it could not borrow money for the benefit of the trust the property was reconveyed to him to make the improvements and then to be reconveyed to the trust. Moreover, it was agreed that the Davenport home had been transferred to the trust by mistake and had not been intended to be a part of the trust at that time. It also was reconveyed to the trustor. (R. 32-33.) Both reconveyances were made despite the provision of the trust indenture that no part of the trust estate could be withdrawn. (R. 96.)

After the creation of the Foundation on July 8, 1940, the board of trustees of the trust adopted a resolution directing La Verne College to convey the trust property to the Foundation and this was done on October 8, 1940. The resolution provided that the conveyances and transfers should be made subject to the trust indenture of May 23, 1939, and that the acceptance of the property by the Foundation "shall be a recognition of the fact that the assets so trans-

ferred are subject to and accepted by this corporation, subject to the terms and provisions of said Declaration of Trust". (R. 33-34.)

On or about May 31, 1941, Levi M. Davenport and his wife transferred the "home place" to the Foundation and contemporaneously entered into an agreement with it under which (a) they retained the right to use the home place for their lives, and (b) the Foundation agreed to pay Lucile Davenport Weller an annuity of \$100 per month and upon her death to pay her daughter, Dorothy Mae Weller, an annuity of \$100 per month. The Foundation's obligation to pay these annuities was absolute and not dependent upon whether the Foundation had net income or net earnings. The annuity to Dorothy Mae Weller was to be reduced under certain conditions not material to this case. The value of the home place on the date of transfer was \$15,500 and its fair rental value was \$1,500 per annum. No rent was ever paid to the Foundation for its use but during the taxable years Mr. Davenport turned over to the Foundation \$432.25 which was part of the money he received from renting rooms in the Davenport home (R. 78), and the Foundation paid taxes and other expenses of upkeep on it, amounting in the years 1941 through 1944, to \$4,206.63. (R. 34.)

On or about May 31, 1941, Levi M. Davenport and his wife transferred the "First Street property" to the Foundation and contemporaneously entered into an agreement with it under which Levi M. Davenport reserved the net income from the property for his life and the right to designate, in writing, during his

lifetime the disposition of the net income for a period not to exceed ten years after his death. This designation was not made by Mr. Davenport. The value of the "First Street property" at May 31, 1941, was \$40,000, and its fair rental value was \$5,400 per annum. The Foundation never received any income from this property and while Mr. Davenport paid the taxes for the years 1940 through 1944, expenses of upkeep for those years, amounting to \$1,720.12, were paid by the Foundation. (R. 35.)

During the taxable year 1940, the Foundation paid Lucile Davenport Weller \$1,000 for the benefit of Levi M. Davenport in connection with his acquisition of certain shares of stock of L. M. Davenport Company, a separate corporation which was dissolved about the time the Foundation was organized (R. 66, 69), and in 1941 it paid Homer Davenport the amount of \$625 for the same reason. The stock held by Lucile Weller and Homer Davenport was surrendered to Levi M. Davenport. (R. 36.) In each of the taxable years 1941 through 1944 the Foundation paid Lucile Weller the amount of \$1,200 pursuant to the terms of the annuity agreement of May 31, 1941. (R. 36-37.)

During the taxable years the Foundation had net income amounting to \$38,484.39, and paid out amounts aggregating \$20,124.09, to organizations and institutions exempt from taxation under Section 101 (6) of the Internal Revenue Code. (R. 37.) During the same period the Foundation paid out \$518.68 to organizations not established as exempt under that provision of the Internal Revenue Code. (R. 35-36.)

The Foundation filed returns for the years involved, claiming exemption from taxation in accordance with the provisions of Section 101 (6) of the Internal Revenue Code, which exemption was denied by the Commissioner. (R. 10.) Later it amended its petition for redetermination of the deficiency assessed by the Commissioner to include a claim of exemption under Section 101 (14) of the Code. (R. 23-25.) The Tax Court decided that the Foundation was not exempt from taxation pursuant to the provisions of Section 101 of the Code (R. 37) and the Foundation here seeks review of that action (R. 44-51).

#### SUMMARY OF ARGUMENT

The statute provides that corporations to be exempt must be organized and operated exclusively for religious, charitable or educational purposes and that no part of its earnings may inure to the benefit of any private individual. The Foundation was not so organized and operated because one of the dominant purposes of the trust under which it was created was the provision made by the trustor for himself and members of his family. There were provisions for the payment of specified sums for religious and educational purposes but no provision that net earnings above those specified should be used for religious, charitable or educational purposes.

Payments were made from net earnings to private persons and for private purposes. These payments were not made from reservations or exceptions against trust property so that none of the rights ever belonged to the Foundation but were charges against its whole income.



Nor is the Foundation exempt under Section 101 (14) of the Internal Revenue Code. It was not organized exclusively to hold title to property and turn over the entire net proceeds to an exempt organization as required by that provision of law. It was not under any legal obligation to turn over any of its funds to any exempt organization and did in fact indiscriminately distribute part of its net earnings to non-exempt organizations and private persons.

#### ARGUMENT

##### I

**The purposes for which the Foundation existed and the use of its funds denied it exemption under Section 101 (6) of the Internal Revenue Code**

Section 101 (6) of the Internal Revenue Code (Appendix, *infra*) under which the Foundation first (R. 10), and apparently principally, claims exemption from taxation provides that religious, charitable or educational corporations, funds or foundations must be “organized \* \* \* exclusively” for those purposes in order to be entitled to exemption and that no part of its net earnings may inure to the benefit of any private individual. We must, therefore, examine into the purpose of the Foundation here, and the use of its earnings, to determine whether it was organized for reasons which bestow exemption upon it and operated accordingly.

The Tax Court in its opinion stated that one of the dominant purposes of the trust was the provision made by the trustor for himself and the members of his family. (R. 39.) It concluded that “since the trust was created for private as well as for public purposes,

all the income of the trust corpus was not to be devoted exclusively to charitable purposes" and that the Foundation had not met the test prescribed in the statute. (R. 42.)

This conclusion is well established by the evidence. It must be borne in mind that the Foundation is the successor, and for that matter, the creature, of the trust indenture made by Levi M. Davenport with La Verne College on May 23, 1939 (R. 84-98), and that it inherited all the obligations of that agreement (R. 33-34). That instrument stated no purposes for which the trust was operated and the articles of incorporation of the Foundation (R. 114-121) state only that it shall act as trustee under "Christian Educational, Charitable, Eleemosynary, and other charitable trusts \* \* \* in accordance with the respective trusts \* \* \*". The trust instrument did, however, specify how net income was to be distributed and the first and opening paragraph under that section specified that \$400 per month was to be paid to the trustor for life. (R. 85.) The third paragraph of that section of the trust instrument specifies that \$100 per month shall be paid to the trustor's brother, and it provides further that his children shall be provided for in the event they come to want. (R. 86.)

These provisions carved out of the net income of the trust a total of \$500 per month for wholly private purposes, and more if the condition of private persons occasioned or warranted it. This amount compares with only \$300 a month for educational purposes in the second paragraph of the same section of the trust instrument and the equivalent of only \$25 a month in

the fourth paragraph. (R. 86.) This demonstrated to the Tax Court the dominant private and family purposes of the trust upon which it denied exemption.

There would seem to be no doubt that the trustor was a religious person and was motivated by religious and charitable considerations in providing for the Department of Philosophy and Religion at La Verne College, but it is highly significant, in view of the detail with which that department was discussed in the trust instrument (R. 87-88), and the qualifications of trustees were detailed (R. 90-91), that the trust instrument carried no other specifications of religious, charitable or educational institutions to which net income was to be distributed except the sum of \$300 per annum to the American Bible Society out of an income producing estate valued at approximately \$270,000 (R. 29). This fact would indicate that religious, charitable or educational considerations were not the exclusive purpose in setting up the trust.

These factors, are not altered by what happened in the operation of the trust. There is no positive evidence that the payments to the trustor and members of his family were waived despite the Foundation's claim to the contrary here. (Br. 25.) Mr. Allard expressed it merely as his opinion that Mr. Davenport had waived the right to the \$400 annuity when he transferred the "First Street property" to the Foundation (R. 55), but he testified he had no conversation with the corporation about it (R. 57) and that he had had no discussion with the brother or children about the matter and obtained no written release of their rights (R. 59). Mr. Steinour, the

treasurer of the Foundation (R. 59), and only other witness who testified concerning the \$400 annuity to Mr. Davenport, stated on direct examination that the earnings of the "First Street property" were in lieu of the annuity, according to his discussion with Mr. Davenport (R. 63), but on cross-examination he also seemed to be expressing opinion as to waiver of the annuity (R. 65). In any event, there was no written instrument waiving the right either of Mr. Davenport or any member of his family to the specified annuities or discretionary amounts, and the liability under the trust instrument remained at all times an outstanding, and apparently enforceable, obligation against the net income from the trust estate. Moreover, the trust instrument provided that the trust was irrevocable and that none of the trust estate could be withdrawn. (R. 96.) The reconveyance was therefore invalid and could have no effect on the provisions of the trust instrument.

In addition to the obligations which were not of a public nature and which meant that net earnings of the Foundation inured to the benefit of private individuals, it was found by the Tax Court that the Foundation made two payments out of its funds which were clearly outside the scope of the claimed exemption. These were the payments to Lucile Weller and to Homer Davenport of \$1,625 for stock surrendered by them to Levi M. Davenport. (R. 36.) There is no evidence to support the Foundation's contention here (Br. 27) that upon dissolution of the company, whose stock he so acquired, he transferred its assets to the Foundation subject to payment for the stock,



and the fact that it was surrendered to him when the dissolution of the company took place earlier indicates that the payment by the Foundation was a payment for him. This was, in any event, therefore, a use of net income for the benefit of a private individual, a situation precluded by Section 101 (6) if exemption is to be obtained.

Moreover, the rather indiscriminate contribution of various sums to various nonexempt organizations, even though small in amount (R. 36), indicates that there was no definite plan or program on the part of the Foundation to foster and support a particular religious, charitable or educational purpose, but rather to use the net income as the trustor, in his individual capacity, desired. This is borne out by the testimony of the secretary of the Foundation that Mr. Davenport, the trustor, directed where the contributions were to be made. (R. 72.) Indirectly, therefore, unallocated net income of the Foundation inured to his, a private individual's benefit and this defeats exemption under Section 101 (6).

It is clear that the Tax Court could reach no other conclusion in this case than that the Foundation was not exempt under Section 101 (6). It has relied in its decision upon *James Sprunt Benevolent Trust v. Commissioner*, 20 B. T. A. 19, and *Scholarship Endowment Foundation v. Nicholas*, 106 F. 2d 552 (C. C. A. 10th), certiorari denied, 308 U. S. 623. These cases are clearly in point.

In the *James Sprunt Benevolent Trust* case, *supra*, the trustee, as in the instant case, set up a trust providing for the payment annually of specified amounts

to certain religious and educational institutions but as the first stated purposes, also as in the instant case, provided for the support and maintenance of male descendants of his parents as ministers of the gospel. He also provided for the private relief of any worthy lineal descendants of his parents and an honorarium for each of the trustees. The honoraria were paid in the taxable year and amounts were paid to the educational institution but no payments were made to or on behalf of the trustor's family. The trust claimed it was exempt from taxes under a provision of the Revenue Act of 1921 identical with Section 101 (6) of the Internal Revenue Code. The Board of Tax Appeals held that the trust was not exempt because it was not organized exclusively for religious, charitable and educational purposes but primarily and principally for the support of members of the trustor's family in the ministry and for the private relief of other members of his family. These benefits were limited to blood relatives of the trustor and that exclusion of the public, the Board held, bars exemption. The parallel between that case and the instant case is apparent and the Tax Court was correct in similarly deciding this case.

The *Scholarship Endowment Foundation* case, *supra*, is almost on all fours with the instant case. There, one Rastall, his wife and one other person in 1932 organized a nonprofit corporation to aid and assist students and others to secure an education. Rastall transferred to the Foundation \$34,000 in stocks and bonds in the same year in consideration for which the Foundation agreed in writing to pay all of the

net income therefrom to the donor during his life and after his death to his wife during her life. In 1934 a new agreement was entered into under which the donor relinquished all rights and interests in and to the securities and in consideration thereof the Foundation agreed to pay him annually during his life the sum of \$5,000 and after his death to pay that amount annually to his wife, during the balance of her life. Rastall made subsequent donations of securities to the Foundation, and in 1936 the value of the donations so made was \$130,000 and in 1937, \$165,000.

No scholarships were awarded in 1932 or 1933 and those in 1934, 1935 and 1936 were \$100, \$200 and \$1,000, respectively. The gross income in 1936, the taxable year involved in that case, was \$15,700, and after making deductions including annuity payments to the donor, the net income was \$10,075. The donor actually drew on account of the annuity during that year only \$2,000. The Foundation claimed it was exempt from taxation under Section 101 (6), but the court denied it was entitled to the exemption. In the course of its opinion the court said (p. 553):

It is plain that the Foundation must meet two requirements in order to come within the ambit of the statute and be entitled to exemption under its provisions. It must be a corporation organized and operated exclusively for educational purposes, and none of its net earnings shall inure to the benefit of any private individual.

The court recognized, without deciding, that under the provisions of the original contract reserving the net income to the donor and his wife, the Foundation merely acted as a conduit for the receipt and transmission of the income and did not fall outside the statute for that reason. It pointed out, however, that the new contract was in force and effect throughout the years in question. Under its provisions the Foundation acquired from the donor the right to receive the income in ownership and in consideration therefor it obligated itself to pay him annually a specified sum during the remainder of his life and thereafter to pay the same amount to his wife during the balance of her life. The obligation was definite and certain in amount and time of payment. The entire assets of the Foundation, both capital and earnings, were unconditionally charged with the obligation and during the period in question payments out of earnings were actually made to the donor on such obligation. It seems clear, the court said, that a part of the earnings thus inured and were devoted to the benefit of a private individual within the intent and meaning of the statute, and that in result the Foundation was not entitled to the exemption for which it contends. That case is authority upon which the decision of the Tax Court in the instant case should be affirmed.

The Foundation in this case pitches its case on the erroneous ground that each of the provisions with respect to the payment of annuities or other amounts, either in the original trust indenture or subsequent agreements, was a reservation and an exception from the properties transferred by the trustor to the Foun-



dition. (Br. 23, *et seq.*) Conceding, as did the court in *Scholarship Endowment Foundation, supra*, that such reservations and exceptions might alter the result in this case, it is clear that there were no such reservations or exceptions here. The only actual reservation was the right, in the original trust indenture, of the trustor to use and occupy the home place rent free for life. (R. 92.) That reservation was vitiated by the subsequent reconveyance of the home place to the trustor (R. 32-33), assuming that, despite the provision of the trust indenture that none of the trust estate might be withdrawn (R. 96), that reconveyance was not invalid. When the home place was conveyed to the Foundation on May 31, 1941 (R. 34), the initial reservation was again reserved but the contemporaneous annuity agreement to pay a stipulated amount to the trustor's daughter and granddaughter was not a reservation against that property. The Foundation received no rent from it (R. 34) and the Tax Court said, as did the Court in the *Scholarship Endowment Foundation* case, *supra*, that the Foundation's obligation to pay these annuities was absolute and not dependent upon whether it had net income or net earnings.

We have pointed out that the situation respecting the "First Street property" was invalid and did not alter the trust agreement. It is also here contended by the Foundation that the additional agreement at the time of the conveyance of this property that the trustor could dispose of the income from the property for a period of ten years after his death by a written document, was in lieu of the right and power of the

trustees, under the original indenture, to provide for the trustor's brother and children in case of want. (Br. 24.) Since at the time of conveyance to the Foundation there was no waiving of rights by trustor's brother and children to part of the income from the trust property (R. 41); no written agreement that those provisions were rescinded and no designation by the trustor of use of income from the property after his death (R. 35), it is clear that those provisions of the trust indenture were not altered and that they contained at all times a direct and complete obligation against the trust income. The transfer of the "First Street property" to the Foundation reasserted the trustor's original intention of procuring an income for life from the trust property for himself and of providing against want and need for members of his family.

It is apparent, we submit, that the Foundation is in error in asserting that all the rights remaining in or going to the trustor and his family were reservations or exceptions from the deeds of property to the Foundation or the predecessor trust, and that as a matter of law none of those rights ever belonged to the Foundation. Its reliance therefore upon *Lederer v. Stockton*, 260 U. S. 3; *Emerit E. Baker, Inc. v. Commissioner*, 40 B. T. A. 555; *Estate of Whitehead v. Commissioner*, 3 T. C. 40, affirmed *sub nom. Commissioner v. Citizens and So. Nat. Bank*, 147 F. 2d 977 (C. C. A. 5th); *Pasadena Methodist Foundation v. Commissioner*, decided October 11, 1943 (1943 P-H T. C. Memorandum Decisions, par. 43,451); *Home Oil Mill v. Willingham*, 68 F. Supp. 525 (N. D. Ala.), and

other authorities cited (Br. 21) is misplaced since in those authorities there was an actual reservation or the right of an organization to acquire trust property fully by discharging an obligation. The Tax Court in its opinion has shown the inapplicability of the rule of the *Stockton* and *Baker* cases, *supra*. (R. 39-41.) None of those cases are authority upon which the decision of the Tax Court may be reversed while the cases of *James Sprunt Benevolent Trust v. Commissioner*, *supra*, and *Scholarship Endowment Foundation v. Nicholas*, *supra*, are authorities supporting the Tax Court's decision that the Foundation is not an exempt corporation under Section 101 (6) of the Internal Revenue Code.

## II

**The Foundation was not organized exclusively to hold title to property, collect income therefrom and turn over the entire amount less expenses to an exempt organization and is therefore not exempt under Section 101 (14) of the Internal Revenue Code**

The Foundation contends in the alternative that if it is not exempt from taxation under Section 101 (6) of the Internal Revenue Code it is exempt under Section 101 (14). This section provides that a corporation which is organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof less expenses, to an organization which itself is exempt from tax, is exempt from taxation. The Tax Court held that it was not exempt under this section because, as the record clearly shows, a portion of its income was distributed to organizations or persons not exempt

from tax. That is sufficient to defeat the Foundation's claim since the statutory provision specifies that the entire amount of net income must reach exempt hands, but another point is significant.

The trust does not provide nor indicate that a particular organization, an exempt organization, to use the words of the statute, or particular organizations should receive the entire amount of the net income from the trust property, nor does it actually specify who or what organization or organizations shall receive the net amount over and above specified annuities and grants. The use of the net amount was left to the sole discretion of the trustees (R. 115) and they, under the direction of the trustor and in accordance with his wishes (R. 72), distributed some but not all of it indiscriminately as contributions among several, not only one, exempt organizations (R. 37), and several nonexempt organizations (R. 35), and to private persons (R. 36) and for private purposes (R. 34, 35). Thus it is seen that there was no intention that the Foundation was organized to get net income into the hands of an exempt organization.

In the case of *Banner Building Co. v. Commissioner*, 46 B. T. A. 857, exemption under Section 101 (14) was denied for that reason. The Board, in deciding that case, said (p. 863) that a holding company under that paragraph is one which has been organized for the exclusive purpose of holding title to property, collecting the income therefrom and turning over the entire amount, less expenses, to an exempt association and that the taxpayer had not shown that it was organized for any such purpose. The taxpayer in



that case contended that actual operations rather than corporate form, were the test of its rights to exemption. The Board, while stating that the record in the case did not show compliance in respect to operations, disposed of this position by stating (p. 864) that an essential requirement of a holding company under the paragraph pleaded is that it turn over income from property held, less expenses, to an exempt association and that the taxpayer had not shown it was under any legal obligation to turn over any of its funds to an exempt association nor had it shown that it did in fact pay over any of its funds to such an association. The failure in that essential, the Board held, precludes classification as an exempt corporation under Section 101 (14). In *N. P. E. F. Corp. v. Commissioner*, decided April 29, 1946 (1946 P-H T. C. Memorandum Decisions, par. 46,100), the Tax Court allowed the exemption where that essential was met.

In the instant case the Foundation was under no legal obligation to turn over any of its funds to an exempt organization and the *Banner Building Co.* case, *supra*, supports the decision in this case. The record, in addition to showing that \$20,000 went to various exempt organizations, shows that substantial sums (R. 34, 35, 36) went for nonexempt purposes.

The Foundation here (Br. 34) pleads the doctrine of *de minimis* to avoid the effect of non-exemption to it under Section 101 (14), but in so doing it refers only to amounts contributed to organizations the status of which was not established. Even if those were the only objectionable items, the rule would not aid the Foundation in view of the clear language of the

statute, but it is not only those items which have effect in the decision of this case. It is also those amounts which went to private persons and for private purposes and these, amounting to over \$12,000 in the taxable years, as pointed out above, are too substantial to be helped by the *de minimis* doctrine.

Moreover, the Foundation asserts (Br. 35) that if any unauthorized distribution has been made this will not defeat exemption because it will recoup them against the trustor. Unauthorized distribution might not defeat exemption if it otherwise existed but recoupment here will not aid the Foundation since it is not, as required by the statute, obligated to pay all of its net earnings into exempt hands.

#### CONCLUSION

The decision of the Tax Court is correct and should be affirmed.

Respectfully submitted.

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GEORGE A. STINSON,

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AUGUST 1948.

## APPENDIX

### Internal Revenue Code:

#### SEC. 101. EXEMPTIONS FROM TAX ON CORPORATIONS.

The following organizations shall be exempt from taxation under this chapter—

\* \* \* \* \*

(6) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation;

\* \* \* \* \*

(14) Corporations organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof, less expenses, to an organization which itself is exempt from the tax imposed by this chapter;

\* \* \* \* \*

(26 U. S. C. 1946 ed., Sec. 101.)

Treasury Regulations 103, promulgated under the Internal Revenue Code:

SEC. 19.101.1. *Proof of exemption.*—A corporation is not exempt merely because it is not organized and operated for profit. \* \* \*

The words “private shareholder or individual” in section 101 refer to individuals having a personal and private interest in the activities of the corporation. \* \* \*

\* \* \* \* \*

When an organization has established its right to exemption, it need not thereafter make a return of income or any further showing with respect to its status under the law, unless it changes the character of its organization or operations or the purpose for which it was originally created. \* \* \*

\* \* \* \* \*

SEC. 19.101 (6)–1. *Religious, charitable, scientific, literary, and educational organizations and community chests.*—In order to be exempt under section 101 (6), the organization must meet three tests:

(1) It must be organized and operated exclusively for one or more of the specified purposes;

(2) Its net income must not inure in whole or in part to the benefit of private shareholders or individuals; and

(3) It must not by any substantial part of its activities attempt to influence legislation by propaganda or otherwise.

Corporations organized and operated exclusively for charitable purposes comprise, in general, organizations for the relief of the poor. \* \* \*

An educational organization within the meaning of the Internal Revenue Code is one designed primarily for the improvement or development of the capabilities of the individual. \* \* \*

Since a corporation to be exempt under section 101 (6) must be organized and operated exclusively for one or more of the specified purposes, an organization which has certain religious purposes and which also manufactures and sells articles to the public for profit, is not exempt under section 101 (6) even though its property is held in common and its profits do not inure to the benefit of individual members of the organization. \* \* \*



A corporation otherwise exempt under section 101 (6) does not lose its status as an exempt corporation by receiving income such as rent, dividends, and interest from investments, provided such income is devoted exclusively to one or more of the purposes specified in that section.

Sections 29.101-1, 29.101 (6)-1 and 29.101-2 as added by T. D. 5381, 1944 Cum. Bull. 188, of Treasury Regulations 111, promulgated under the Internal Revenue Code, applicable to years beginning after December 31, 1941, are substantially identical with the quoted provisions of Treasury Regulations 103.



No. 11,912

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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THE DAVENPORT FOUNDATION,

*Petitioner,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

---

REPLY BRIEF ON BEHALF OF PETITIONER.

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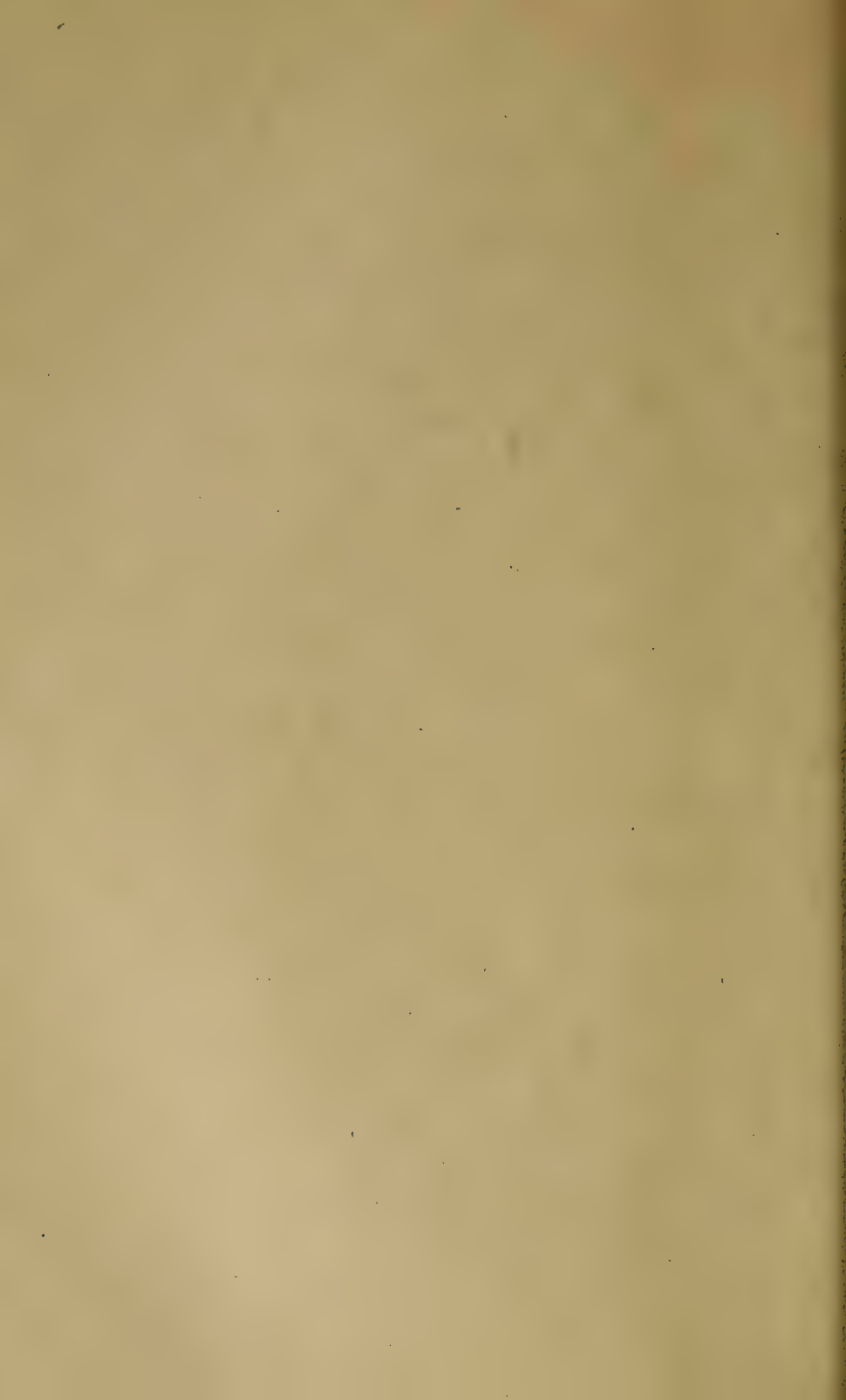
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FILED

AUG 20 1948





## TOPICAL INDEX.

	PAGE
Comment on respondent's statement of facts.....	1
Reply to respondent's argument.....	4
I.	
Petitioner is exempt under Section 101(6) of the Internal Revenue Code .....	4
II.	
Petitioner is exempt under Section 101(14) of the Internal Revenue Code .....	17
Conclusion .....	19
Appendix. Statement showing net income from property trans- ferred by Levi M. Davenport to Davenport Foundation to December 31, 1944.....	App. p. 1

## TABLE OF AUTHORITIES CITED.

CASES	PAGE
Banner Building Co. v. Commissioner, 46 B. T. A. 857.....	17
Edward Orton, Jr. Ceramic Foundation, 9 T. C. 541..10, 11, 12, 15	
Emerit E. Baker, Inc., 40 B. T. A. 555, Acquiescence 1940-1, C. B. 1 .....	12
Eppa Hunton, 1 Tax Court 821.....	16
James Sprunt Benevolent Trust, 20 B. T. A. 19.....	14, 15
Kirby Petroleum Co. v. Commissioner and Commissioner v. Crawford, 326 U. S. 599.....	10
N. P. E. F. Corp. v. Commissioner, decided April 29, 1946 (1946 Prentice Hall Tax Court Memorandum Decisions, par. 46,100)..	18
Scholarship Endowment Foundation v. Nicholas, 106 F. (2d) 552 .....	13
Whitehead, J. B., Estate of, v. Commr., 3 T. C. 40, affd. 147 F. (2d) 957 .....	10, 15
William C. Bruckner, 20 C. T. A. 419.....	17

## STATUTES

Internal Revenue Code, Sec. 101(8).....	3
Internal Revenue Code, Sec. 101(14).....	18, 19
Internal Revenue Code, Sec. 191(6).....	4

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---

**REPLY BRIEF ON BEHALF OF PETITIONER.**

---

**Comment on Respondent's Statement of Facts.**

The general picture presented by the respondent's statement of facts resembles the one which appeared in the petitioner's statement of facts but respondent has omitted certain facts which it is believed should be in mind in determining whether petitioner is exempt from tax.

Respondent did not state that Levi M. Davenport transferred substantially all of his property to La Verne College [Tr. 34], or that he never accepted any of the \$400.00 monthly payments provided for by the original trust [Tr. 62, 64], or that petitioner has never paid any amount for the support of the brother or sons of Levi M. Davenport [Tr. 65, 150], or that the brother and children of petitioner were so fixed financially that they would not be likely to ever call upon petitioner for as-

sistance [Tr. 67-71, incl.]. Furthermore, respondent did not state that any payment to the trustor's brother was to be discretionary with the Trustees [Tr. 86].

Petitioner believes that the evidence shows that petitioner took the assets subject to the debts or claims owing to the daughter and son of Levi M. Davenport in the amount of \$1,000.00 and \$625.00, respectively [Tr. 66-70, incl.].

Petitioner believes that the evidence shows that the annuity agreements of May 31, 1941, created obligations of petitioner which were to be in lieu of obligations set up in the original trust indenture. Reference to the evidence on this point is made at pages 8 and 9 of petitioner's original brief. The respondent suggests that any change in the original obligations would have constituted a partial withdrawal or revocation by Mr. Davenport or perversion of the trust, but it should be noted that this change was not a unilateral action by Mr. Davenport but a bilateral agreement entered into between Mr. Davenport and petitioner in which, presumably, new obligations equal to the old obligations were set up.

Finally, the respondent's figure of \$518.68 paid by petitioner to organizations not established as exempt under the Code, is erroneous. See page 7 of respondent's brief. At the beginning of the trial a stipulation was filed, that certain facts were true but that evidence could be introduced at the trial not contradictory thereto. The stipulation stated that the taxpayer had paid \$518.68 to organizations for which no known exemption from income



tax had been granted. Then at the trial testimony was introduced which showed that the following contributions were to tax exempt organizations:

Phillips China Relief [Tr. 63, 64, 65]	\$150.00
Radio Gospel Hour (Dr. M. H. Fagan)	
[Tr. 72]	85.00
Flora, Evangelist [Tr. 72]	8.00
	<hr/>
Total	\$243.00

It was further stipulated that \$19,881.09 was contributed to organizations which were known to be exempt from income tax [Tr. 79]. The Tax Court then found that \$20,124.09 had been contributed to organizations exempt from income tax. This was made up of the \$19,-881.09, stipulated on page 79, and the \$243.00 as to which testimony was given at the trial. This then would take the \$243.00 out of the \$518.68 and reduce it to \$275.68. Then out of the \$275.68 should come the \$50.00 paid to the Property Owners' Association of California as a business expense. Furthermore, that Property Owners' Association was exempt from income tax under provisions of Section 101(8) of the Internal Revenue Code [Tr. 81]. Hence, the contributions made to organizations with no known income tax deductions, aggregated \$225.68 rather than \$518.68.

## REPLY TO RESPONDENT'S ARGUMENT.

### I.

#### Petitioner Is Exempt Under Section 101(6) of the Internal Revenue Code.

The purpose for which petitioner and its predecessor were organized was to give to charity and religious education all of Mr. Davenport's property except bare necessities of life for himself and his wife for life, a small annuity for his daughter, and a possibility of a slight provision for the other members of the grantor's family.

Mr. and Mrs. Davenport had an estate of approximately \$270,000.00. The income from this was more than sufficient to provide for their support. His fortune was adequate to provide substantial legacies to his children. If those uses of the property had been his chief concern, he would simply have kept the property and not formed petitioner or its predecessor.

But Mr. Davenport wished to give to charity everything excepting a bare living for himself and wife, with a little protection, for lives in being, of his brother and children. But thereafter everything was to belong to the charitable organization. The amounts reserved by Mr. Davenport for himself and family were less than the income of the trust, leaving to the charitable trust and the corporation, the entire corpus and some of the income for the first few years, and all of the income after lives in being.

The entire record leaves no doubt but that the above represent the purpose for which the trust and the corporation was formed. The dominant purpose of petitioner and its predecessor was to extend religious education. The grantor transferred the trust property to a denomination-

al college and appointed as trustees the president of the college, two ministers, a daughter of the trustor, and one other person. The trust indenture provided that a department of philosophy and religion would be established and would be supported out of the trust income. It also provided for an annual payment to the American Bible Society. Then, after making provision for the support of the trustor and wife for life, with discretionary power to give assistance in case of want to his brother and children, he provided that the rest of the income should be distributed as determined by the Board of Trustees for the purposes consistent with the purposes of the trust. The type of religious education to be taught is fully set out in the trust indenture. The indenture provided that all of the successor trustees of the trust had to be approved by the Elders' Body of the Church of the Brethren of the District of Southern California and Arizona, and each such person so approved had to be a person who, by his life and conduct, could subscribe to a very strict code of moral ethics and that such a trustee might be removed if he became unfit to serve by becoming ethically or scripturally embroiled in the evil things of the world. In arranging for the compensation for the trustees the trust instrument stated that it was hoped that all those having to do with the management of the Foundation would have the sacrificial spirit, in order that the work set up by the trust would grow and prosper. The indenture also provided that others might add to the foundation provided additional income should be used in maintaining the doctrines and principles of the Church. It further provided that should La Verne College fail to establish this department of philosophy and religion, and to carry out the teachings as enunciated, or it should be merged or consolidated with any other educational or charitable institution or cease to

exist, then the trustees should pay the income therein provided to be paid to it, to some other institution within the same church denomination, and a new trustee would take the power of La Verne College as title holder. In the by-laws it was provided [Tr. 107] that the Board of Trustees of the Foundation should send an annual report of the business of the Foundation to the District Conference of the Church of the Brethren of the District of Southern California and Arizona not later than 20 days before the annual meeting of said District Conference.

The Articles of Incorporation of petitioner stated that its purpose was to act as trustee under Christian, educational, charitable, eleemosynary and other charitable trusts, and to operate without pecuniary gain or profit to the members. Vacancies on the Board of Directors of petitioner were to be filled by the Elders' Body of the Church of the Brethren, with the same qualifications as were required by the trustees of the predecessor trust. Hence, the trust indenture, the Articles of Incorporation and the history and background of the transaction, show that the trust property was irrevocably devoted to the *kind* of a charity specifically prescribed in the case of La Verne College.

As to the *operations* of the trust and the corporation. all of the income, excepting the amount necessary for the bare maintenance and support of the grantor and his wife and daughter, was either distributed to charitable, religious and educational organizations or invested in additional property. The grantor, Levi M. Davenport, managed the property of petitioner without salary. He even turned over to the petitioner money he received from renting out one of the rooms in the Davenport home [Tr. 78]. Neither the brother nor the sons of Levi M. Daven-



port ever received anything from this trust or petitioner, excepting the \$625.00 Homer Davenport received for his interest in the assets transferred to petitioner's predecessor.

Perhaps the best test of the dominant purpose of the petitioner and predecessor is to determine whether the most money or property was available for the charitable or the private use. Attached hereto, as an appendix, is a statement showing the net income from the property transferred by Levi M. Davenport to the petitioner and its predecessor to December 31, 1944; also the amounts which were reserved by or paid over to Mr. Davenport and his wife and daughter, as well as the balance remaining. The record shows that the petitioner and predecessor received property of the value of \$270,384.00 [Tr. 76, 78] and the exhibit in the appendix shows that the property produced a net income up to December 31, 1944 of \$70,409.87; a grand total of \$340,793.87. The same exhibit will show that Mr. Davenport, his wife and daughter received from the beginning of the trust until December 31, 1944, money, or use of property, having an aggregate value of \$31,875.00. If there is added in, contrary to petitioner's conviction, the \$1,625.00 paid to the daughter and son of Mr. Davenport, for assets transferred to petitioner, the total amount the family received up to December 31, 1944, was \$33,500.00. This is less than half the income. The same proportion no doubt prevailed in 1945 and 1946 and until Mr. Davenport's death on January 6, 1947 (Mrs. Davenport died in 1943).

This would leave, as of January 6, 1947, petitioner in possession of the original capital \$270,384.00, plus more than half the income from October 8, 1940 to January 6, 1947, and subject only to the following:

1. An annuity to Mr. Davenport's daughter of \$100.00 per month which, of course, equals a small portion only of the income of the property. From January 1, 1947, to the end of her expectancy this would hardly exceed \$18,400.00 in the aggregate.

2. The possibility, as contended by respondent, that further amounts of income might be paid out to the brother and children of Mr. Davenport. Petitioner believes that these rights have been cut off and further points out that any payments to the brother and children is discretionary with the Board of Trustees. The brother, John R. Davenport, was, on February 28, 1947, 71 years of age. He testified that he had property worth \$18,000 or \$20,000, net, and received about \$200 per month from it, and that he had no dependents or children, and that his property was sufficient to keep him. Ralph M. Davenport, son, on January 1, 1947, was about 51½ years of age, had received \$35,000 from his father, had an important position with the gas company, received a very good salary, lived in a large house and did not have a large family. Homer H. Davenport, son, was about 45 years of age on January 1, 1947, was married and had no children. He was worth about \$30,000. His property was producing considerable income. He was not otherwise employed and was in poor health. Lucille D. Weller, the daughter, was nearly 54 years of age on January 1, 1947, was married to an able-bodied man and had a married daughter who was not dependent on her. The income of her husband and

herself was more than enough to take care of them. Her husband and herself were worth \$85,000 to \$100,000.

If Homer Davenport became in need of assistance, and if the Board of Trustees of petitioner decided to help him, such assistance would not exceed a small portion of petitioner's income, and then for a few years only. Thereafter, petitioner would own, free and clear of all encumbrances and liabilities, the assets worth \$270,000.00 in 1939, and probably worth a great deal more in 1947. The property was producing a net income of around \$18,500 a year in 1944, and it will probably keep up at that rate indefinitely.

Consequently, petitioner has received up to January 6, 1947, net assets and net income, over and above the amount it has paid or will have to pay therefor, of at least \$300,000.00.

The figures tell the story. They demonstrate the dominant purpose of the trust and of the creation of petitioner and of the transfer of the property to it. The figures show that the grantor's purpose was to give everything he had to charity, excepting a frugal existence for himself and wife for the few remaining years of their lives and a small annuity to his daughter. In other words, he intended to give all he possibly could, and still sustain life.

Petitioner and its predecessor received property subject to certain conditions, reservations and exceptions. The faithful performance of these conditions was a condition to its obtaining the property—a part of the purchase price of the property. It is not material that these requirements on behalf of the grantor technically amounted to reservations and exceptions. The net effect determines

the point and in the case at bar Mr. Davenport transferred the property to the trust and the corporation in consideration of certain reservations and certain trust income. He reserved those rights and the corporation never received those rights. It only received the balance. In *Kirby Petroleum Co. v. Commissioner* and *Commissioner v. Crawford*, 326 U. S. 599, the Supreme Court held that a lessor who was to get a portion of the net income realized from the operation, by the lessee, of the oil well, retained an economic interest in the property entitling him to depletion deductions, and that the lessee did not own such portion of the operating income. That decision is cogent authority for this proposition that the rights to income retained by Mr. Davenport amounted to reservations or exceptions from the property interests transferred to petitioner.

The Supreme Court case of *Lederer v. Stockton*, 260 U. S. 3, is of course the leading authority on the proposition that property transferred to a charitable organization subject to a reservation, does not deprive the organization of its exemption.

The following cases are authority for the proposition that the exemption is not destroyed because of the fact that the charitable organization pays out portions of *net income* to the nominees of the grantor. *Estate of J. B. Whitehead v. Commr.*, 3 T. C. 40, affirmed 147 F. (2d) 957, and *Edward Orton, Jr. Ceramic Foundation*, 9 T. C. 541.

In the *J. B. Whitehead* case, *supra*, the net estate of the decedent was left to a charitable foundation. The will provided that two annuities aggregating \$15,000 per year



would be paid *out of income* for 20 years. The foundation and estate were also to settle contracts with testator's wife and former wife. Exemption was granted despite the fact that some of the income was paid to private persons and this annuity was not a charge on capital but was merely to come out of income.

In the *Edward Orton, Jr. Ceramic Foundation* case, *supra*, there was created by will a foundation to run a cone business for educational purposes. Out of the income of the foundation, testator's wife or issue were to get specific sums each year for five years, totaling \$42,000.00. These amounts were not payable in all events or out of corpus, but merely out of the income. Nevertheless, the Tax Court held that the foundation was exempt. There the Tax Court said:

"The payments of income to the wife, both under the will and under the agreement, were not the real purpose for which the foundation was established. They were a charge upon its entire assets and had to be paid in order to free the assets and income for use in the scientific aims of the foundation. In this respect the facts were indistinguishable from those in *Emerit E. Baker, Inc.*, 40 B. T. A. 555, where we held that a corporation, otherwise entitled to exemptions from income tax under section 101(6) of the Revenue Acts of 1934 and 1936, was not deprived of the exemption because of payment of an annuity to his widow \* \* \*. In the instant case the income-producing property all belongs to the foundation, and if the foundation should cease to exist it will all go to Ohio State College after the death of the life annuitant."

As shown by the above cases, it is immaterial whether a charitable foundation gets property subject to a specific annuity, which is a charge on all income and assets, or merely subject to the payment of certain amounts out of income, or portions of the income. In either case, it has to pay the amounts in order to free the assets from obligations so that they can be devoted to certain charitable purposes.

The real test then, in this type of case, is not whether some of the assets or income must be paid to private persons but whether the dominant purpose is to provide for charitable uses, or to make provision for private persons. In that connection the dominant purpose cannot be determined by the purpose which is first set forth in the trust indenture, as argued by the respondent on page 10 of his brief. In the case of *Emerit E. Baker, Inc.*, 40 B. T. A. 555, Acquiescence 1940-1, C. B. 1, the first purpose stated in the will was a provision for the benefit of the testator's wife. Nevertheless, The Tax Court properly held that this was not the dominant purpose of the trust. It was merely incidental to the dominant purpose of providing for charity. Likewise, in the case at bar the fact that the first provision for the distribution of income was the matter of \$400 for the support of the grantor, does not mean that was the dominant purpose of the trust. The Tax Court said in *Edward Orton, Jr. Ceramic Foundation*, 9 T. C. 533, page 541:

"The basis for distinguishing these cases must be found in the general purpose and history of the trusts or foundations under consideration. Where, as in the instant case, the evidence shows a clear and predominant purpose to aid the charity and where the noncharitable benefits are incidental to that purpose,

we think that the exemption should be allowed. As stated in *Helvering v. Bliss*, 293 U. S. 144: “\* \* \* The exemption of income devoted to charity and the reduction of the rate of tax on capital gains were liberalizations of the law in the taxpayer’s favor, were begotten from motives of public policy, and are not to be narrowly construed \* \* \*.”

That the dominant motive of the grantor in *Scholarship Endowment Foundation v. Nicholas*, 106 F. (2d) 552, cited by respondent, was to provide for the grantor is shown by the fact that in 1934 when the trust had property worth \$34,000 only, the indenture was amended to provide an annuity of \$5,000 per year for the life of the grantor and his wife. Previously, he had reserved all the income for the life of the donor, and after his death to his wife during her life. These arrangements showed that the grantor did not intend that the charity should get anything during the life of his wife or himself. Thereafter, and at the beginning of the taxable year 1936, he did contribute an additional \$130,000 in property, but out of gross income in 1936 of nearly \$16,000, only \$1,000 was distributed for scholarships, and \$5,000 was available to the grantor and his wife, although he drew only \$2,000 during that year. The Court was justified in holding that during the life of the grantor and his wife the dominant purpose of the trust was to pay them all of the income, or even more than the income.

As the District Court said, 25 Fed. Supp. 511, page 514:

“Under the first contract the donor was to receive the entire income leaving nothing for charitable objects. Then a new agreement was entered into still more favorable to him \* \* \*.”

Respondent also cites The Tax Court decision in *James Sprunt Benevolent Trust*, 20 B. T. A. 19, which held that the trust was not exempt from income tax. In that case, in the preamble of the trust instrument, the trustor stated that he had had a yearning for many years to provide for the temporal support of a son or a grandson, or a blood relation, who would be called to the Gospel Ministry of the Southern Presbyterian Church. In stating the purposes of the trust he said:

“The first and primary purpose of this trust is, as hereinbefore mentioned, to provide any direct male or female descendant of my parents, \* \* \* who is also a member of the Southern Presbyterian Church, who may make application to this Board, with funds for preparation, and partial or full support in the ministry of the Gospel, or in Missionary work at home or abroad under the Southern Prersbyterian Church, \* \* \*. It is my desire that in such case the trustees shall provide the cost of such preparation and subsequent support, on *liberal lines*, and in the event of the death of any beneficiary leaving a dependent family it shall be the duty of the Trustees to make suitable provision at their discretion, \* \* \*.”

Later in the trust he also provided that one-fifth of the income would be used for the private relief or assistance of any worthy lineal descendant of Alexander Sprunt and Jane Dalziel Sprunt, regardless of their church affiliation. The trustor in that case did not put in a limit on



the amount that could be spent for the support of his relatives who were studying for the ministry and did provide that 20% of the income was to be used for the support of other relatives. These payments were to begin immediately. He then made some provisions for charitable uses which were to begin after his death. In addition he provided that 10% of the income of the trust would be paid out for the support of underpaid Presbyterian ministers and further provided that the trustees should pay \$50,000.00, when convenient, to the Davidson College. These last two items were apparently to begin immediately. The capital contributed to the trust was \$500,000.00, par value, of 7% debentures. While the Board of Tax Appeals would have been justified, under the present test, of holding that the trust was not exempt because its dominant purposes were private benefits rather than charitable uses, it actually used a test which ignored the principle established by the Supreme Court in *Lederer v. Stockton*, 260 U. S. 3, that the exemption would not be lost even though some of the income went for private use, if this portion was incidental to the dominant charitable purposes. It will be noted that The Tax Court in the *James Sprunt Benevolent Trust* case did not refer to *Lederer v. Stockton*. The more recent cases, such as the *J. B. Whitehead*, *Emerit E. Baker* and *Edward Orton, Jr. Ceramic Foundation* cases take into consideration the principle enunciated in *Lederer v. Stockton*, and permit some distribution of income to private persons but allow exemption if the dominant purpose is charitable.

Respondent says on page 13 of his brief that the fact that Mr. Davenport directed where the contributions were to be made, meant that such portion of the income inured to him and this defeated the exemption. But in *Eppa Hunton*, 1 Tax Court 821, the trust indenture provided that the grantor's wife would have the sole right of designating the beneficiaries during her life. The Tax Court there did not consider that this amounted to a distribution for her benefit, and held the trust was exempt from income tax.

Petitioner and its predecessor received \$270,000.00 worth of property and are entitled to keep all the income therefrom in consideration for allowing to the grantor and his wife and daughter, and perhaps his brother and sons, some small portion of the company's income for a limited period of time. Thereafter the corporation would have the property and its income free from any obligations, free to advance Christian education and otherwise invest in charitable and educational and religious purposes. It received, taking everything into consideration, a very substantial gift from Mr. Davenport for charitable purposes.

Petitioner has expended all its income, left to it after paying the amounts required to enable it to receive the property, for charitable purposes, except such portions as it accumulated for expanding its property.

The dominant function is a charitable and educational and religious one and, therefore, exemption follows.

II.

**Petitioner Is Exempt Under Section 101(14) of the Internal Revenue Code.**

As shown in the preceding portion of this brief, petitioner was organized for the dominant purpose of carrying on educational, religious and charitable work and has used all of the funds available to it, after payments required of it by the grantor, for such purposes. Payments have been made only to organizations exempt from income tax, excepting a very small amount which should be ignored under the *de minimis* doctrine. Any unauthorized payments will be recouped by petitioner.

The fact that petitioner accumulated some of its income for the purpose of increasing or improving its properties, hence creating more income for charitable and educational purposes, does not deprive it of exemption. See *William C. Bruckner*, 20 C. T. A. 419.

The respondent, on page 20 of his brief, cites the case of *Banner Building Co. v. Commissioner*, 46 B. T. A. 857. The corporation there involved was a private business corporation organized for profit. Its by-laws provided that the profit would be distributed to the stockholders. It raised capital by selling stock to members of a lodge, erected a building, and rented the building out to the lodge. The facts are so clearly distinguishable that they will not be further considered.

Respondent argues on page 20 of his brief that the trust indenture in the case at bar does not specify what exempt organization is to get the balance of income left over after provisions have been made for the trustor, La Verne College and the American Bible Society, and the brother and children of the trustor. Respondent con-

cluded that there was no intention that the Foundation be organized to get net income into the hands of an exempt organization.

But in *N. P. E. F. Corp. v. Commissioner*, decided April 29, 1946 (1946 Prentice-Hall Tax Court Memorandum Decisions, par. 46,100), the Tax Court allowed exemption under Section 101(14) of the Internal Revenue Code where the taxpayer's *operations* satisfied the test of the statutory requirement that it be "organized" and "operated" for charitable purposes but the charter did not specify that the net income was to be paid to some exempt organization. The Commissioner in that case argued that the N. P. E. F. Corp. was not exempt as it was not "organized" to turn net income over to exempt organizations, even though it actually did so. The Tax Court said:

"But the statements upon which respondent relies for this proposition contained in *Sun-Herald Corporation vs. Duggan* (C. C. A., 2nd Circuit), 73 Fed. (2d) 298 (4 U. S. T. C., par. 1355), certiorari denied, 294 U. S. 719, were repudiated by the same court in *Roche's Beach, Inc. vs. Commissioner* (C. C. A. 2nd Circuit), 96 Fed. (2d) 776, (381 U. S. T. C., par. 9302)."

Therefore, petitioner in the case at bar distributed, or accumulated for later distribution, all the income available to it, after making the payments required in order to obtain the property, to exempt organizations. It is exempt under Section 101(14) even though the trust indenture does not specifically set forth the name of the organization to which the excess income is to be paid.

The respondent on pages 21 and 22 of his brief seems to concede that \$200 or \$300 which petitioner paid to



non-exempt organizations can be ignored under the *de minimis* doctrine. He suggests however, that the petitioner is claiming that the amounts going to the members of the trustor's family should also be ignored under the *de minimis* rule. Petitioner does not make that claim as it feels that the amounts going to the trustor's family, went by virtue of reservations or exceptions and were payments required to be made by petitioner in order to obtain the property.

Respondent also apparently concedes on page 22 that the recoupment of unauthorized distributions would save petitioner's exemption.

Petitioner, therefore, was organized and operated to turn over all of its own net income to organizations exempt from tax. It is exempt under Section 101(14) of the Internal Revenue Code.

### Conclusion.

The decision of the Tax Court is erroneous and should be reversed.

Respectfully submitted,

MELVIN D. WILSON,  
*Counsel for Petitioner.*

August 27, 1948.









NO. 11913

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IN THE  
United States  
Circuit Court of Appeals  
For the Ninth Circuit

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GEORGE HARRISON MEEKS,  
*Appellant,*

*vs.*

UNITED STATES OF AMERICA,  
*Appellee.*

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*Appellee's Brief*

*On Appeal From the District Court for the  
Territory of Alaska, Division Number One.*

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## INDEX

	Page
TITLE OF CASE .....	1
PRELIMINARY STATEMENT .....	1
FACTS .....	2
ISSUES:	
I. Argument Answering Specification I .....	6
II. Argument Answering Specification II .....	12
III. Argument Answering Specification III .....	22
IV. Argument Answering Specification IV .....	27
CONCLUSION .....	36

## STATUTES CITED

### COMPILED LAWS OF ALASKA, 1933:

Section 4757 .....	1, 5
--------------------	------

### ALASKA COMPILED LAWS ANNOTATED, 1949:

Section 58-4-58 .....	14
Section 58-4-59 .....	6
Section 65-4-1 .....	5

### FEDERAL RULES OF CRIMINAL PROCEDURE:

Rule 17 (b) .....	22, 24, 37
18 U.S.C.A. SECTION 563 .....	23
18 U.S.C. SECTION 3005 .....	23
28 U.S.C.A. SECTION 656 .....	22, 25
UNITED STATES CONSTITUTION AMEND. VI .....	23

## CASES CITED

	Page
Alleman v. Stepp, 52 Ia. 627, 3 N.W. 636 .....	30
Aplin v. United States (CCA-9) 41 F 2d 495 .....	14
Ann. Cases 1914 B. 1122, 1123 .....	7
Arnold v. United States (CCA-10) 94 F 2d 499 .....	10
Austin v. United States (CCA-9) 19 F 2d 127, Cert. Den. 275 U.S. 523 .....	25
Bailey et al v. State (Sup. Crt. Ala.) 53 So. 296 .....	18
Birmingham So. Ry. Co. v. Lintner, 141 Ala. 420, 38 So. 363, 109 Am. St. Rep. 40 .....	32
Brewer, et al v. United States (CCA-9) 150 F 2d 314 .....	26
Casebeer v. Hudspeth, Warden (CCA-10) 121 F 2d 914, Cert. Den. 317 U.S. 704 .....	23, 24, 27
Clark v. State (Crt. Cr. App. Tex.) 148 S.W. 801 .....	21, 26
Coats v. State 101 Ark. 51, 141 S.W 197 .....	29
Cochran v. United States, 157 U.S. 286, 39 L ed. 704, 15 Sup. Crt. 628 .....	32
Commonwealth v. Morrow, 3 Brews. (Pa.) 402 .....	8
Crumpton v. United States, 138 U.S. 361, 364 .....	24
Dupuis v. United States (CCA-9) 5 F 2d 231 .....	25, 27
Eldridge v. State (Sup. Crt. Fla.) 9 So. 448 .....	19
Eugee v. State (Sup. Crt. Ga.) 126 S.E 471 .....	21, 27
Figueroa v. State (Crt. Cr. App. Tex.) 159 S.W. 1188 .....	21, 26
Gates v. United States (CCA-10) 122 F 2d 571, Cert. Den. 314 U.S. 662 .....	26
Goldsby, alias Cherokee Bill v. United States 160 U.S. 70..	24, 27
Harrold v. Territory of Oklahoma (CCA-8) 169 F 47 .....	14
Hackins v. State (Sup. Crt. Ala.) 103 So. 468 .....	19
Johnston v. Jones, 1 Black (U.S.) 210, 17 L Ed. 117 .....	32
Kettenbach, et al v. United States (CCA-9) 202 F 377, 378 .....	14
Kuhn et al v. United States (CCA-9) 24 F 2d 910, Reh. Den. 26 F 2d 463, Cert. Den. 278 U.S. 605 .....	35



	Page
Lau Fook Kau v. United States (CCA-9) 34 F 2d 86....	18, 21, 26
McDuffie v. State (Sup. Ct. Ga.) 49 S.E. 708 .....	18, 21, 27
McFalls v. State 66 Ark 16, 48 S.W. 492 .....	29
McRaye v. United States (CCA-9) 163 F 2d 868 .....	14
Meeks v. United States (CCA-9) 163 F 2d 598 .....	1, 11
Mode v. State, 169 Ark. 356, 275 S.W. 700 .....	29
Pandula v. Fonseca (Sup. Ct. Fla. Sec. B) 199 So. 358....	16, 19
People v. Becker, 215 N.Y. 126, 109 N.E. 127, 210 N.Y. 274, 104 N.E. 396 .....	11
People v. Carnavelle, 196 N.Y.S. 56 .....	10
People v. Elco, 131 Mich. 519, 91 N.W. 755, 94 N.W. 1069	8
People v. Louis Berardi, et al (Sup. Ct. Ill.) 163 NE. 668	14
People v. Michaels (Sup. Ct. Ill.) 167 N.E 857 .....	18
People v. Minsky, 227 N.Y. 94, 124 N.E. 126 .....	10
People v. Moore (Sup. Ct. Mich.) 10 N.W. 2d 296 .....	34
People v. Strauch (Sup. Ct. Ill.) 93 N.E. 126 .....	21, 27
People v. Vertrees (Sup. Ct. Cal.) 146 P 890 .....	18, 21, 27
Perkins v. State (Sup. Ct. Ark.) 271 S.W. 326 .....	17
Re Dolbeer, 149 Cal. 227, 86 P 695 .....	32
Riddle v. United States (CCA-5) 279 F 216, Cert. Den. 259 U.S. 586 .....	13, 17
St. Louis and San Francisco Ry. Co. v. Bishop (Sup. Ct. Ark.) 33 S.W. 2d 383; Cert. Den. 283 U.S. 854 .....	18
Sasser v. State (Sup. Ct. Ga.) 59 S.E. 255 .....	21, 27
Shailer v. Bullock, 78 Conn. 65, 61 A 65 .....	32
Sneed v. State (Sup. Ct. Ariz.) 14 P 2d 248 .....	21, 26
Stanley v. State (Ark.) 297 S.W. 826 .....	28
State v. Baird (Sup. Ct. Vt.) 65 Atl. 101 .....	16
State v. Bissell (Sup. Ct. Vt.) 170 Atl. 103 .....	16
State v. Coleman (Sup. Ct. N.C.) 2 S.E. 2d 865 .....	13
State v. Coomer, 105 Vt. 175, 163 A 585, 94 ALR 1038 ....	29

	Page
State v. Harrison, 66 Vt. 523 .....	9
State v. Henry (Sup. Crt. Wash.) 254 P 460 .....	18
State v. Hines (Sup. Crt. Ore.) 34 P 2d 921 .....	19
State v. Magoon, 50 Vt. 333 .....	9
State v. Scott (Supr. Crt. Mo.) 58 S.W. 2d 275 .....	34
State v. Slack 69 Vt. 486, 38 Atl. 311 .....	8
Thompson v. Owen, 174 Ill. 229, 51 N.E. 1046 .....	7
Tucker, et al v. United States (CCA-8) 5 F 2d 818 .....	14
United States v. Ball, 163 U.S. 662 .....	15, 16
United States v. Best (D.C. Mass.) 76 F Supp. 138 .....	26
United States v. Hall, 44 F 864, 10 LRA 324 .....	7, 8
United States v. Manton, et al (CCA-2) 107 F 2d 834, Cert. Den. 309 U.S. 664 .....	14
Vassar v. Chicago, B and Q Ry. Co. (Sup. Crt. Nebr.) 236 N.W. 189, 74 ALR 1154 .....	15, 19
Williams v. Walker, 19 SC Eq. (2 Rich.) 291, 46 Am. Dec. 33 .....	7
Wright v. City of Anniston (Ala.) 44 So. 151 .....	13, 17
Young v. United States (CCA-5) 97 F 2d 200, Reh. Den. 97 F 2d 1023 .....	36

## TEXTBOOKS

58 Am. Jur. Sec. 624 .....	32
58 Am. Jur. Sec. 629 .....	14
58 Am. Jur. Sec. 715 .....	15
58 Am. Jur. Sec. 792 .....	7
58 Am. Jur. Sec. 795 .....	8
58 Am. Jur. Sec. 863 .....	29
22 C.J. Sec. 1227 .....	12
Wigmore on Evidence 3rd Ed. Sec. 934 .....	30, 31
Wigmore on Evidence 3rd Ed. Sec. 951 .....	20
Wigmore on Evidence 3rd Ed. Sec. 2425 .....	11

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IN THE

United States

Circuit Court of Appeals

For the Ninth Circuit

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GEORGE HARRISON MEEKS,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

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Appellee's Brief

PRELIMINARY STATEMENT

Appellant, who was the defendant below, was convicted of the crime of Murder in the First Degree in violation of Section 4757, Compiled Laws of Alaska, 1933, and on appeal to this Court said Judgment of Conviction was reversed. *Meeks vs. United States*, No. 11293, 163 F 2d 598 (CCA-9, 1947). Following a retrial in the District Court for the Territory of Alaska, Division Number One, at Juneau, the appellant was again adjudged guilty of the crime of First Degree

Murder based upon the verdict of a jury pursuant to which appellant was sentenced by the Honorable George W. Folta, presiding, to imprisonment for life.

## FACTS

On Monday, December 10, 1945, the body of Clarence J. Campbell was found in a ditch on the outskirts of the City of Juneau, Alaska. There were cuts and bruises on his head and face and a very deep laceration of his throat which completely severed the trachea and left carotid artery.

The victim, Campbell, who was a contract shingler, had arrived in Juneau only a few days before his death, from Hoonah, Alaska, to do shingling on the new Juneau Federal Housing Development Project. Campbell was known to have been carrying on his person slightly more than \$2100.00 consisting mostly of hundred dollar bills and a smaller number of fifty dollar bills on Saturday and Sunday, December 8 and 9, 1945; but when his body was found on the following day, December 10, 1945, several of his pockets were turned inside out, and all of his money as well as his wrist watch was missing.

Meeks, the appellant, was shown to have been in Juneau since the latter part of October, 1945, and to have been without funds and borrowing money to live on up until Sunday evening, December 9, 1945, the day before Campbell's body was discovered and shortly after he was seen in company with Campbell. The



purely fortuitous discovery of this money in appellant's possession was not only tremendously significant because of the amount being similar to that stolen from Campbell, but it was also in the same denominations as the bills Campbell was possessed of prior to his being robbed and murdered. The appellant even borrowed money from one Eddie Schwaesdall to pay for his transportation to Juneau, although after the murder he lied about this to a Federal investigator and wrote to Schwaesdall requesting him to deny making the loan if questioned about it. Appellant requested an advance on wages due him from a temporary job and received the total amount due him, namely \$8.00, on December 8, 1945. In making request for this advance after working only one day he stated to his employer that he was broke and needed money for food over Sunday, December 9, 1945. Also on Saturday, December 8, 1945, appellant propositioned one Kelso Hartness, suggesting that they hit "a big shot from Hoonah" over the head and take away his money as this man had over two thousand dollars in hundred and fifty dollar bills.

The discovery hereinabove referred to of a large amount of money in appellant's possession was quite by chance, and was made at about 9:30 on the night of December 9, 1945, while Juneau Police Officers were investigating a disturbance at the Keystone Rooms in response to a call by the landlady. It was discovered at this time that appellant Meeks had in his possession a large number of hundred dollar bills

and Meeks gave the officers a one hundred dollar bill "for their trouble." Later that night he displayed seventeen one hundred dollar bills, four fifty dollar bills, two twenty dollar bills and two ten dollar bills, to Kelso Hartness and Lena Brown, according to the testimony of these persons, as well as appellant's own admission. Hartness also testified that on the same Sunday evening, December 9, appellant, after displaying the money in a boastful manner, borrowed a clean shirt from Hartness and the two of them went to the public toilet down the hall and there Meeks removed his shirt which had blood stains on it and put on the shirt he borrowed from Hartness after tearing up his own and flushing it down the toilet. Percy Reynolds, the owner-operator of a restaurant in Juneau, testified that late Sunday evening, December 9, 1945, Kelso Hartness, whom he knew by his having worked for him and eaten at his restaurant, came to his restaurant and during his purchase told him (Reynolds) of a fellow being up in his room with a whole lot of money, over \$1900.00.

In addition, it was shown that appellant knew the deceased who had the adjoining room to him in the Keystone Rooms in Juneau; that the two were together on Sunday evening, December 9; that they were seen at about 7:00 P.M. walking together in the direction where Campbell's body was found; and that at about 7:30 P.M. two people answering their description as to size were seen approaching the lonely spot where Campbell's body was discovered. Later Meeks

denied ever knowing Campbell, and attempted to pay for the transportation of one John Kalinowski, who had seen the two together, in order to have Kalinowski leave town so he could not testify.

On Monday, December 10, 1945, when Meeks was questioned as to the money which he had acquired so suddenly the previous night, a pair of wet trousers was found in his room. Appellant said he had washed these trousers and was going to send them to the laundry. Later it was discovered that there were human blood stains covering a large area of these trousers though the stains were too thin to type due to the washing. Human blood stains were also found on appellant's suit coat.

Shortly after the murder Meeks gave Nathan Skinner a Hamilton wrist watch in payment for a debt, telling Skinner to tell the "F.B.I." it was a watch given him by Meeks before the murder. This Hamilton wrist watch was proved by eye witnesses and by pawn records to have been the property of deceased, and the watch he was wearing up to and just prior to the time his body was discovered.

It was on the evidence outlined above and numerous other circumstances that the appellant was convicted by the verdict of a jury on his re-trial in the District Court for the Territory of Alaska at Juneau of First Degree Murder (without capital punishment), in violation of Section 4757, C.L.A. 1933; Section 65-4-1, A.C.L.A. 1949.

## ISSUES

### I

NO ERROR WAS COMMITTED BY THE TRIAL COURT IN PERMITTING THE PROSECUTION TO EXAMINE ONE OF ITS WITNESSES WITH REFERENCE TO HIS PRIOR CONVICTION OF A FELONY.

Appellant contends that the Trial Court committed prejudicial error in permitting the prosecution to examine in chief Government witness Kelso B. Hartness as to his previous criminal conviction, notwithstanding the fact that the defendant made no objection to this questioning and notwithstanding the further fact that on cross-examination defendant's attorneys examined witness Hartness on the same subject much more fully than the Government on its examination in chief. On cross-examination of Hartness defense attorneys were permitted by the Trial Court to go into the question of punishments and conditions of sentences, including the questioning of Hartness as to his being under control of law enforcement authorities at the time of his testifying. (Tr. 507, lines 7, 8 and 9) (Tr. 507, line 20) (Tr. 508, lines 8 to 11 incl.)

Of the two grounds advanced by appellant in support of his contention the first is based on the fact that a party who calls to the stand a witness cannot impeach that witness, and quotes The Alaska Territorial Statute, Section 58-4-59, Alaska Compiled Laws Annotated, 1949.



Whether or not and under what circumstances a party to litigation may be permitted to impeach his own witness has from the earliest times been a subject of much controversy and of many decisions. 58 Am. Jur. Sec. 792, p. 438. In this country the general rule is well established, that subject to certain exceptions a party may not impeach his own witness. It is respectfully submitted that the circumstances in this case come within one of the exceptions to the general rule stated above.

One of the reasons advanced in support of the rule that a party cannot ordinarily impeach his own witness is that in calling the witness the party vouches for his credibility. But this reason and the rule grounded on it can have no application where the calling of the witness is not voluntary. In fact, a witness whose calling is not voluntary can hardly be called the party's witness—*United Staes v. Hall*, 44 F 864; 10 LRA 324—but is rather a witness of the law. So a party may impeach a witness whom he is compelled to call, or whom by legal intendment he cannot avoid calling, as in the case of an attesting or subscribing witness to a deed or a will.

*Thompson v. Owen*, 174 Ill. 229, 51 NE 1046  
*Williams v. Walker*, 19 S.C. Eq. (2 Rich) 291,  
46 Am. Dec. 33

Likewise, the prosecution in a criminal case may impeach a witness whom it is under a legal duty or obligation to call. Ann. Cases 1914 B 1122, 1123, such

as an available witness to the crime, a witness who has testified before the grand jury, or a witness whom the court compels the prosecution to call. 58 Am. Jur. Sec. 795.

Since a witness whom a party is compelled by law to call or a witness to a crime in a criminal prosecution is not regarded as his witness within the rule which prohibits a party from impeaching his own witness, he may be impeached by such party in the same manner as any other witness. Under this exception to the general rule it has been held that where the prosecution is compelled by the court to put a certain witness on the stand, it may impeach him. *United States v. Hall*, 44 Fed. 864. Also, the obligation of the prosecution to call on the trial a witness who testified before the grand jury has been held to be such as to relieve it from the operation of the rule forbidding impeachment. *Commonwealth v. Morrow*, 3 Brews. (Pa) 402. Similarly, it has been held that it is the duty of the prosecution in a criminal case to produce every available witness to the crime, and the rule forbidding the impeachment of one's own witness has accordingly no application in such cases.

*People v. Elco*, 131 Mich. 519, 91 N.W. 755, 94 N.W. 1069

*State v. Slack*, 69 Vt. 486, 38 Atl. 311

Announcing this rule, the court said in the case last cited:

As the public, in whose interest crimes are prosecuted, has as much interest that the innocent should be acquitted as that the guilty should be convicted, we hold it to be the duty of the State to produce and use all witnesses within reach of process, of whatever character, whose testimony will shed light upon the transaction under investigation and aid the jury in arriving at the truth, whether it makes for or against the accused, and that therefore the State is not to be prejudiced by the character of the witnesses it calls.

*State v. Magoon*, 50 Vt. 333

*State v. Harrison*, 66 Vt. 523

This doctrine, carried to its logical result, exempts the state in criminal cases from the operation of the rule in question, and places it in the position of a party calling an instrumental witness, and for the same reason.

In the case at bar not only was Hartness a witness before the grand jury which indicted the appellant but he was one of the principal witnesses for the plaintiff Government and the only one giving direct testimony of premeditation. Prosecutions are carried on by the Government, through the agency of sworn officers elected or appointed for that purpose, who have no private interests to serve nor petty spites to gratify, but whose sole and only duty is to faithfully execute their trust, and do equal right and justice to the Government and to the accused.

In the case of *Arnold v. United States*, decided in 1938 by the United States Circuit Court of Appeals for the 10th Circuit and reported in 94 F 2d 499, we have a case wherein the United States Attorney in a criminal prosecution interrogated two Government witnesses on their examination in chief concerning their prior convictions of a felony. On cross-examination, when questioned by appellants' counsel as to what felony they had been convicted of, on objection by the United States Attorney, the court sustained same and denied the information as to what felony they had committed. As can be readily understood from a review of the authorities the trial court was reversed for so ruling, but no objection or exception whatsoever was taken to the question of the right of the United States Attorney to examine in chief Government witnesses concerning previous felony convictions and it is respectfully contended that no error was committed in the case at bar in permitting the Assistant U. S. Attorney, where no objection was made, to ask Government witness Hartness on his examination in chief as to his previous conviction of a felony, especially where on cross-examination of the witness defendant's attorneys questioned witness Hartness minutely on the same matter, bringing out the name of the crimes, the sentences and conditions in connection therewith.

In the case of *People v. Minsky*, 227 N.Y. 94, 124 N.E. 126, which was cited with approval in *People v. Carnavelle*, 196 NYS 56, the rule is stated as follows:



The law does not limit a party to witnesses of good character, *nor does it compel a party to conceal the bad record of its witnesses from the jury*, to have it afterwards revealed by the opposing party with telling effect. Such a rule would be unfair alike to the party calling the witness and the jury. Men have been convicted of murder in the first degree by the evidence of admittedly dangerous and degenerate witnesses, law breakers, and professional criminals. *People v. Becker*, 215 N.Y. 126, 109 N.E. 127; 210 N.Y. 274, 104 N.E. 396.  
(Emphasis supplied.)

With reference to the appellant's further contention that proceedings, orders, judgments, and decrees of a court of record cannot be proved by parol, it is submitted that its argument is inapplicable to the facts in issue and deals with the question concerning the general theory of the rule of law against varying the terms of a writing, which is the precise title of Section 2425, Volume IX, of Wigmore on Evidence cited by appellant at the outset of its argument on this subject. Further, appellant's argument on this subject is not germane as the question of proving *terms* of a contract or other document is not here in issue. No attempt was made in this case to vary the terms of a written contract or judicial record, the only question being whether a judgment of a conviction against the witness existed. It is further submitted that no clearer authority concerning the precise point in issue can be found outside of this court's ruling in *Meeks v. United States*, (CCA-9) 163 F 2d 598, when it reversed the

judgment of a conviction for the trial court's refusal to permit alternative methods to be used in showing the prior conviction of a witness. It is submitted that a criminal conviction of a witness may be established by alternative methods, namely, by his examination or by the record of the judgment of conviction.

*Meeks v. United States, Supra.*

Also the existence of a writing as distinct from its contents may be proved by parol,—22 C.J. Sec. 1227, P 986—and where the matter to be proved is a substantive fact which exists independently of any writing, although evidenced thereby, and which can be as fully and satisfactorily established by parol as by the written evidence, then parol evidence may be admitted regardless of the writing.

22 C.J. Sec. 1227, P 983, 984.

## II

THE TRIAL COURT DID NOT COMMIT PREJUDICIAL ERROR IN LIMITING THE CROSS-EXAMINATION OF GOVERNMENT WITNESS KELSO B. HARTNESS AND IN REFUSING TO ADMIT EVIDENCE OF A COLLATERAL ASSAULT.

Appellant complains in his second assignment of error that the Court erred in not permitting defendant

to cross-examine Government witness Kelso B. Hartness as to the particulars of appellant's assault on Hartness January 8, 1946, which was the subject matter in a separate case entitled *United States v. George Harrison Meeks*, No. 2417-B in the District Court for the Territory of Alaska. In this case Hartness was the complaining witness and stated under oath that Meeks assaulted him with a dangerous weapon and inflicted numerous wounds with a knife about his neck, throat and arms. Further witness Hartness testified under oath in the original trial of instant case (original trial Tr. P. 461 to 473) relative to that matter. All of the testimony, without equivocation shows appellant to have been the assailant. That offense occurred approximately one month after the murder of Clarence Campbell, for which appellant was on trial, and thus the facts were wholly independent and collateral to the case at bar.

*Wright v. City of Anniston* (Ala.) 44 So. 151

*State v. Coleman* (Sup. Crt. N. C.) 2 S.E. 2d 865

*Riddle v. United States* (CAA-5) 279 F 216,  
Cer. Den. 259 U.S. 586.

The subject matter, i.e. fight between appellant and witness Hartness in the Gastineau Hotel January 8, 1946, in which appellant inflicted some 27 wounds with a knife, was not inquired into by the Government on direct examination. Therefore the details of that affray were not within the limit and scope of proper cross-examination of Witness Hartness.

Sec. 58-4-58, A.C.L.A. 1949.

58 Am. Jur. p. 349, Sec. 629, Notes 14 and 15.

*People v. Louis Berardi, et al*, (Sup. Crt. Ill.)  
163 N.E. 668

*Harrold v. Territory of Oklahoma* (CCA-8) 169  
F 47

*Aplin v. United States* (CCA-9) 41 F 2d 495

*Kettenbach, et al. v. United States* (CCA-9) 202  
F 377, 387

*McRaye v. United States* (CCA-9) 163 F 2d 868

*Tucker, et al v. United States* (CCA-8) 5 F 2d  
818

*United States v. Manton, et al*, (CCA-2) 107  
F 2d 834, 845, Cer. Den. 309 U.S. 664, where-  
in it is said "The office of cross-examination  
is to test the truth of the statements of  
the witness made on direct; and to this end  
it may be exerted directly to break down the  
testimony in chief, to affect the credibility of  
the witness, or to show intent. The extent  
to which cross-examination upon collateral  
matters shall go is a matter peculiarly within  
the discretion of the trial judge. And his  
action will not be interfered with unless  
there has been upon his part a plain abuse  
of discretion."

The fight between appellant and Hartness on January 8, 1946 is relevant to the case at bar, only in so far as Hartness, being the victim to the assault by appellant, acquired an ill feeling, became biased and hostile, or prejudiced against appellant as a result of the assault, and such ill feeling, bias, hostility, and



prejudice influenced his testimony regarding the guilt or innocence of appellant.

A careful review of the transcript (Tr. Vol. 3, P. 499-524) clearly reveals that appellant sought to place before the jury not the fact of the assault, but the particulars of the collateral offense. That is all that was objected to by the government, and all that the Court ruled out. Obviously appellant was seeking to impeach and discredit witness Hartness' testimony by showing his bias, hostility and prejudice. In such case, the material point was the existence of feeling, bias, hostility and prejudice toward appellant, and not the right or wrong or merits of the transaction which occasioned it.

58 Am. Jur. P 387, Sec. 715, Note 18

*United States v. Ball*, 163, U.S. 662

*Vassar v. Chicago, B. & Q. Ry. Co.* (Sup. Ct. Neb.) 236 N.W. 189, 74 A.L.R. 1154

The only purpose in admitting such testimony in evidence is to enable the jury to weigh and appraise the pertinent facts related by the witness, in the light of his existing hostile feelings, bias and prejudice. Inquiry into this fact, however, does not open up the entire field which motivates the lives of witnesses. Some men would remain friendly in spite of utmost harrassment, while others acquire bitter feelings at the slightest provocation. The only safe standard which the law has devised is whether bias, prejudice and hostile feeling exist, and the extent thereof.

When Hartness' hostile attitude was revealed as near as it actually existed, described as feeling "unkindly", "unfriendly", "just unfriendly toward him; that is all", and not "bitter", but unfriendly (Tr. Vol. 3, p. 518, 519), further examination into the details of the collateral offense ceased to be material and objections thereto were properly sustained.

The rule is well stated in *State v. Bissell* (Sup. Ct. Vt). 170 Atl. 103 where it is said that "ill will or unfriendly feelings of a witness may be shown by a general inquiry whether the witness is friendly or otherwise; but the question is so collateral to the issue that details will not be permitted to be shown." The Court held that refusal to permit the witness for the state to answer whether he tried to reverse a collect telephone call and refuse to accept same, was not error.

*State v. Baird*, (Sup. Ct. Vt.) 65 Atl. 101

*Pandula v. Fonseca*, (Sup. Ct. Fla. Sec. B) 199  
So. 358

A similar rule was expressed by the Supreme Court of the United States in *United States v. Ball* 163 U.S. 662, a murder case, in which the trial court's limitation on cross examination of two government witnesses as to their bias and prejudice was upheld. The Court said: "The court permitted defendant's counsel, for the purpose of showing bias and prejudice on the part of these witnesses, to ask them whether they had, at their own expense, employed another attorney

to assist the District Attorney in the prosecution of the case; and they frankly answered that they had. That fact having been thus proved and admitted, the further question to one of them 'how much do you pay him' might properly be excluded by the presiding judge as immaterial."

In general, it may be said, the fact of a relationship or circumstance from which hostility may reasonably be inferred may be shown, but not its details.

Thus, where a feeling of hostility of the witness against the defendant, because the latter as an attorney had prosecuted the witness' two sons for arson, was admitted, a further inquiry as to whether one of the sons had not pleaded guilty was held irrelevant. *Riddle v. United States*, (C.C.A.-5) 279 F 216, Cer. Den. 259 U.S. 586. No error was committed by the trial court in sustaining objections to the question propounded by defendant to a state witness on cross examination " 'Is it not true that you carried Harry Wright out of the store into the street, and knocked, choked and abused him before you left the store,'—for the obvious reason that it called for the particulars of the difficulty." *Wright v. City of Anniston* (Sup. Crt. Ala.) 44 So. 151.

A case particularly in point is *Perkins v. State* (Sup. Crt. Ark.) 271 S.W. 326, in which error was assigned because the court refused to allow the state witness to state the particular matter which caused her to have ill feeling against defendant. She was asked whether

she had "ill" feeling against defendant and answered "No." Then she was asked if she "disliked" him and replied that she did. In approving the exclusion of further examination into the matter the court said "This was sufficient and the court did not err in refusing to allow her to be asked the particular matter which caused her to dislike the defendant. Her dislike of him, and not the reason for it, would be the cause which might affect her credibility as a witness."

*People v. Vertrees*, (Sup. Ct. Cal.) 146 Pac. 890, and *McDuffie v. State*, (Sup. Ct. Ga.) 49 S.E. 708 are directly in point with the preceding case as well as the case at bar, and sustain the ruling of the trial court.

In the trial of any case the court enjoys considerable discretion to see that the trial is conducted in an orderly manner, to avoid delay, and prevent collateral issue getting before the jury. The extent of cross examination of a prosecuting witness as to interest, bias, hostility, prejudice and collateral issues is especially discretionary with the court, and it is generally said the Court's rulings will not be disturbed on appeal in the absence of abuse.

*Lau Fook Kau v. United States* (CCA-9, 34 F 2d 86.

*Bailey et al v. State* (Sup. Ct. Ala.) 53 So. 296

*People v. Michaels* (Sup. Ct. Ill.) 167 N.E. 857

*State v. Henry* (Sup. Ct. Wash.) 254 P. 460

*St. Louis & San Francisco Railway Co. v. Bishop*,  
(Sup. Ct. Ark.) 33 S.W. 2d 383; Cert. Den.  
283 U.S. 854



*State v. Hines*, (Sup. Ct. Ore.) 34 P. 2d 921

*Blackins v. State* (Sup. Ct. Ala.) 103 So. 468

*Vassar v. Chicago, B. & Q. Ry. Co.* (Sup. Ct. Neb.) 236 N.W. 189, 74 A.L.R. 1154

*Pandula v. Fonseca*, (Sup. Ct. Fla. Sec. B.) 199 So. 358

*Eldridge v. State*, (Sup. Ct. Fla.) 9 So. 448

Examination of the testimony which appellant expected to solicit from cross examination of witness Hartness (Tr. Vol. 2 p. 499 to Vol. 3, p. 518) as revealed in the transcript of the first appeal (Original trial Tr. 461 to 473) reflect appellant was the aggressor and inflicted some 27 wounds on witness Hartness with a knife. Some of these wounds were about the neck and throat. Peter Vincent, another Government witness, testified, without objection, appellant threatened to cut his throat and actually swung at him with a knife (Tr. Vol. 2, p. 297-299~~X~~). The instrument used in the assault on Hartness could easily be inferred by reasonable jurors to be similar to the instrument used in the murder of Clarence Campbell, he having died from severe lacerations about his head and throat. (Tr. Vol. I, p. 176-189.) If such facts tend to magnify Hartness' ill feeling and hostile attitude toward appellant more than was expressed in his own words, he knowing the state of his own mind better than anyone else, it is difficult to comprehend how revelation of the facts before the jury would not also prejudice their minds adversely to appellant's interest. Particularly is this true when considered along with evidence that

appellant did not want the police to know he had \$1500 (Tr. p. 341); and asked John Kalinowski to leave Juneau so he wouldn't testify against appellant, (Tr. Vol. 3, p. 638, 644, 670.) The details of that collateral offense reflect a course of conduct on the part of appellant, conduct of violence, by use of knives in cutting men's throats without cause, to say nothing of justification, with the apparent intent to kill and prevent Hartness from testifying against him. (Tr. Vol. 2, p. 491-492). Avoidance of this undue prejudice is all the more reason why the Court should have sustained objections to the offered testimony, and in doing so, it is respectfully submitted, that the Court did not commit prejudicial error.

Wigmore on Evidence, 3rd Ed. Vol. 3, p. 508, Sec. 951 in discussing the details of quarrels between a witness and a party on cross examination explains that in ascertaining the state of feeling from a quarrel "inconvenience may ensue in two ways: (1) the detailed inquiries, the denials, and the explanations, are liable to lead to multifariousness and a confusion of issues; (2) the detailed facts of the dispute may involve a prejudice to the character of the witness *or of his opponent*, (emphasis added) which it would be desirable to keep out of the case. From this point of view, some line of limitation must be drawn, and an effort made to avoid these drawbacks . . . . Accordingly, it is commonly held that the details of the quarrel or other conduct may be excluded, in the trial Court's discretion." Cases supporting this view and which hold that the details

of an affray, altercation between a person accused of crime and a witness for the prosecution are collateral and irrelevant and may not be shown for the purpose of proving the witness' bias, prejudice and hostility are as follows:

*Clark v. State* (Crt. Cr. App. Tex.) 148 S.W. 801

*Figueroa v. State* (Crt. Cr. App. Tex.) 159 S.W. 1188

*Lau Fook Kau v. United States*, (CCA-9) 34 F 2d 86

*Sneed v. State* (Sup. Ct. Ariz.) 14 P. 2d 248

*People v. Vertrees*, (Sup. Ct. Cal.) 146 P. 890

*McDuffie v. State* (Sup. Ct. Ga.) 49 SE. 708

*Sasser v. State* (Sup. Ct. Ga.) 59 S.E. 255

*Eugee v. State*, (Sup. Ct. Ga.) 126 S.E. 471

*People v. Strauch* (Sup. Ct. Ill.) 93 N.E. 126

The argument that Hartness' motive for testifying in instant case was so appellant would be convicted and he would not have to testify in *United States v. George Harrison Meeks*, No. 2417-B is simply fallacious. If he was fearful of committing perjury by stating the details of that offense consistent with the complaint against appellant in that case, he had already done so, for he had sworn to the fact of the assault in the criminal complaint, and also testified in the first trial of this case as to the facts of that case in detail. (Original trial Tr. p. 461-473) Furthermore, counsel for appellant in arguing the point before the Court (Tr. Vol. III, p. 522-523) suggested "His

motive for testifying in this case is so he will be convicted on the murder charge and No. 2417-B will never have to come up . . . ” Witness Hartness interrupted and answered this by saying “That is not my motive.” (Tr. Vol. III, p. 523, line 16). That adequate opportunity to examine witness Hartnes as to his interest, fear of arrest, bias, hostility, friendship and motive is apparent from the recorded testimony (Tr. Vol. III, p. 502-513, 516, 518, 520-524). If there was failure in this regard it was because counsel did not pursue the subject in a direct and forthright manner. (Tr. Vol. III, p. 517-518, 520-524).

### III

THE TRIAL COURT DID NOT COMMIT PREJUDICIAL ERROR IN DENYING DEFENDANT’S MOTION TO SUMMON DEFENSE WITNESSES TRAFTON, MATHEWSON, AND PETERSON.

Rule 17 (b) of the Federal Rules of Criminal Procedure require that motions to subpoena witnesses for defendants at Government expense be supported by affidavit stating the testimony expected of each witness, “and shall show that the evidence of the witness is material to the defense.” The showing required by this rule to justify such relief is the same as that exacted by 28 U.S.C.A. 656, namely: Name and address of each witness, testimony expected, that the evidence is material to the defense, that defendant cannot safely



go to trial without the witnesses, and is unable to pay the fees of such witnesses. See Note to Subdivision (b) Advisory Committee on Rules of Rule 17. The motion to subpoena James T. Mathewson, Doris Peterson and Raymond Trafton was heard December 26, 1947, at which time the Court required appellant to support this motion by affidavit showing the materiality of the testimony of Peterson, Trafton and Mathewson. No such supporting affidavit appears in the praecipe or anywhere in the record. Nor is there a request for it. An examination of the District Court file (No. 2418-B) fails to reveal any affidavits setting forth the required information. Appellant does not in his brief refer to such an affidavit, or point out the expected testimony. It is quite apparent from these facts that no affidavit as required by law was ever filed to support the motion.

Therefore, appellant not complying with the law by filing supporting affidavits setting forth the names and addresses of the witnesses, substance and materiality of the testimony expected from each was not entitled to the relief sought.

*Casebeer v. Hudspeth, Warden* (C.C.A.-10) 121 F 2d 914, conforming to mandate of Sup. Crt. 312 U.S. 662, Rehearing Den. 317 U.S. 704.

Appellant had a right "to have compulsory process for obtaining witnesses in his favor", United States Constitution, Amendment VI, and (18 U. S. C. A. 563) 18 U.S.C. 3005. This included the issuance and service of process, but did not require pay-

ment by the Government of expenses of the witnesses. *Casebeer v. Hudspeth*, (C.C.A.-10) 121 F 2d 914, Cer. Den. 316 U.S. 683; Rehearing Denied 317 U.S. 704.

The Court in instant case did not refuse to issue a subpoena and afford compulsory attendance of witnesses in favor of appellant. It only refused to require their attendance at Government expense. The duty of the Court in this regard has been defined several times by the Supreme Court and Appellate Courts. In every instance it has been held that refusal to grant the relief sought in instant case "at Government expense" was wholly discretionary with the Court.

The Supreme Court of the United States in *Goldsby, alias Cherokee Bill v. United States*, 160 U.S. 70 stated that "the right to summon witnesses at the expense of the Government is by the statute, Rev. St. No. 878, left to the discretion of the trial Court, and the exercise of such discretion is not reviewable here." *Crumpton v. United States*, 138 U.S. 361, 364, which expressed a similar view is cited as authority.

Both the statutory language and court interpretation of the previous and existing law applicable here vest the trial court with discretion, which is not subject to review by the appellate court.

Rule 17 (b) of Federal Rules of Criminal Procedure, aside from judicial interpretation, makes it discretionary with the trial courts in affording compulsory attendance of witnesses, at Government expense, in behalf of indigent defendants. The language is clear

from the first sentence of the rule which provides "The court *may order* (emphasis added) at any time that a subpoena be issued upon motion or request of an indigent defendant." This language is similar to the law 28 U.S.C.A. 656, in force at the time of the adoption of the Rule. Pertinent language in that statute was that the court "*may order* that such a witness be subpoenaed if found within the limits aforesaid." (emphasis added). The present law though phrased differently, changes the former law only by extending the place of service of the subpoena to any place within the United States, instead of former limitations of within the district in which the court was held, or within 100 miles of the place of trial. See note to Subdivision 17 (b) of Rule 17 of Federal Rules of Criminal Procedure. The discretionary authority of the court in refusing such compulsory attendance of witnesses for defendants at Government expense has not been changed. Then by giving meaning and effect to Rule 17 (b) it must be interpreted as 28 U.S.C.A. 656 has heretofore been construed by the Courts.

*Dupuis v. United States* (C.C.A.-9) 5 F 2d 231 in construing 28 U.S.C.A. 656 held refusal of the trial court to procure the attendance of a witness in favor of the defendant, at Government expense, not error, said "That the matter of such procurement was within the discretion of the court, is both statutory and settled by the Courts."

*Austin v. United States* (C.C.A.-9) 19 F 2d 127,

Cert. Den. 275 U.S. 523 held failure to subpoena a witness for defendant at Government expense was "not subject to review by an appellate Court."

Other cases holding refusal of trial Courts to grant such relief is a matter for the trial Courts discretion are:

*Brewer, et al v. United States* (CCA-9) 150 F 2d 314

*Gates v. United States* (CCA-10) 122 F 2d 571, Cert. Den. 314 U.S. 662.

*United States v. Best* (D.C. Mass.) 76 F. Sup. 138

The suggestion by appellant in his brief that the expected testimony of Raymond Trafton, James T. Mathewson and Doris Peterson was material is answered under Issue II of this brief. The evidence alluded to by counsel appears to have been the testimony of these witnesses in the first trial. All of that evidence with the exception of Raymond Trafton relates to the details of the altercation between appellant and witness Hartness January 8, 1946, which was held not admissible as evidence to show interest, bias, prejudice or hostility of the Government witness.

*Clark v. State* (Crt. Cr. Ap. Tex.) 148 S.W. 801

*Figueroa v. State* (Crt. Cr. Ap. Tex.) 159 SW 1188

*Lau Fook Kau v. United States* (CCA-9) 34 F 2d 86

*Sneed v. State* (Sup. Ct. Ariz.) 14 Pac. 2d 248



*People v. Vertrees*, (Sup. Ct. Cal.) 146 Pac. 890  
*McDuffie v. State* (Sup. Ct. Ga.) 48 S.E. 708  
*Sasser v. State* (Sup. Ct. Ga.) 59 S.E. 255  
*Eugee v. State* (Sup. Ct. Ga.) 126 S.E. 471  
*People v. Strauch* (Sup. Ct. Ill.) 93 N.E. 126

Appellant cannot complain of the absence of witness Raymond Trafton, in view of his failure in complying with the law in seeking his attendance as a witness, and further, in view of the Court's discretion in requiring his attendance at Government expense, the exercise of which is not subject to review.

*Casebeer v. Hudspeth, Warden* (CCA-10),  
Supra

*Goldsby, alias Cherokee Bill v. United States*,  
Supra

*Dupuis v. United States* (CCA-9), Supra

Furthermore, no contention was ever made, nor is it made now on appeal, that Raymond Trafton would furnish evidence other than that related by him in the first trial of the case. His testimony given in the first trial was available and in fact was read to the jury (Tr. P. 912) upon an agreed stipulation between the prosecution and the defendant.

#### IV

NO PREJUDICIAL ERRORS WERE COMMITTED BY THE TRIAL COURT AND THE DEFENDANT RECEIVED A FAIR AND IMPARTIAL TRIAL UNDER THE ADVERSARY THEORY OF LITIGATION.

(1) The appellant complains that the opening statement of the United States Attorney to the jury at the outset of the trial wherein he made reference to the case being up for re-trial after reversal on a legal technical matter amounted to a denial of substantive rights of the defendant. It is submitted that these words were not improper, that they were intended only to explain to the jury the reason for re-trying a previously convicted accused, and that under no circumstances could any other impression reasonably be gained by the jury.

It has been held not only proper but necessary for a prosecuting attorney on the re-trial of a case in his opening statement to tell the jury of the previous conviction of accused and reversal by an appellate court.

*Stanley v. State* (Ark) 297 S.W. 826

The Supreme Court of Arkansas said in *Stanley v. State*, Supra:

The object of the statement is to enable the court and jury to more readily understand the issues to be tried and the evidence subsequently adduced.

Likewise, much discretion as to what may be stated by the prosecuting attorney is given to the trial court. The trial court should always see to it that the prosecuting attorney acts in good faith in making his opening statement.

*McFalls v. State* 66 Ark. 16, 48 S.W. 492

*Coats v. State* 101 Ark. 51, 141 S.W. 197

*Mode v. State* 169 Ark. 356, 275 S.W. 700

It is respectfully submitted that on the facts and the law the trial court did not abuse its discretion in the case at bar.

(2) The appellant's second point under its fourth and last general specification of error concerns the trial court's allowing the prosecution to "elicit" testimony from Government witness Hartness which differed from his testimony at the first trial, with reference to the particular time of day of a certain occurrence. The fact that there is some conflict in the testimony of a witness does not deprive it of its probative value.

*State v. Coomer* 105 Vt. 175, 163 A 585, 94 ALR 1038

The question presented by conflict between testimony of a witness and his statements, made at some other time or in some other trial is one of his credibility which belongs to the province of the jury.

58 Am. Jur. Sec. 863, P 492

Since the testimony referred to as "elicited" was adduced in the regular procedure of the trial on his examination every opportunity to cross-examine the witness as to the discrepancy between his former testimony and his present was available as well as the right to properly comment thereon in argument.

(3) Since appellant's third point under its fourth general specification of error is substantially a restatement of its specification of Error No. II, we refer to our answer to specification of Error No. II, in this brief. Appellant further states that the attitude of the trial court and its several rulings in favor of the Government resulted in deprivation of a fair trial to the accused, without attempting to specify the rulings it refers to, and without citing authorities in support of its assertion. It is most strongly denied that the rulings of the trial court were based on a mistaken view of the law and it is respectfully contended rulings of the trial court were in accordance with the law and fair and proper.

(4) Appellant contends in his fourth point under his specification of Error No. IV that the trial court committed prejudicial error in limiting cross-examination of witness Lena Brown as to her physical condition at times other than those concerned with events relating to her testimony and beyond the limit of matters brought out on direct examination. In support of their contention they cite Wigmore on Evidence, Vol. III, Section 934 and the case of *Alleman v. Stepp*, 52 Ia. 627; 3 N.W. 636 cited under said section, which deals generally with evidence of diseased impairment of the testimonial powers, drug addicts and mental derangements. The apparent attempt to picture witness Lena Brown as a diseased and mentally deranged person or possibly as a drug addict is not borne out by the record. As to the length of her illness, which regardless of the



primary cause resulted in an upset stomach and vomiting, the record reflects she was ill about two days, December 8 and 9, 1945, and was well on Monday, December 10, 1945. On cross-examination Lena Brown testified, "I wasn't sick Friday." (Tr. P. 595 Line 16) Also on cross-examination when questioned, "When did you get well?" She testified, "Monday afternoon." (Tr. P 595 Line 12, 13) When questioned on cross-examination about having taken tablets she testified as follows:

"Did you say you were sick and had taken tablets and were asleep?" (Tr. P 593 Line 24, 25) Lena Brown replied: "I did later." (Tr. P 594 Line 1) With further reference to the record Lena Brown testified, "—— The doctor gave me some pills for my nerves and for me to sleep, and I took *one*, I believe. I don't remember when——." (Tr. P 596 Line 2, 4)

It is respectfully submitted that the facts in the case at bar do not warrant the finding that witness Brown was suffering from any diseased impairment of her mental faculties or that she was a morphine or other drug addict, as discussed in *Wigmore* at Section 934 and cited by appellant.

Lena Brown testified concerning Sunday evening, December 9, that she was "Just sleepy. I was all tired out." (Tr. P 596 Line 22)

It is submitted that the trial court was most liberal in permitting a searching cross-examination of Lena

Brown as to her physical and mental condition and in its sound discretion committed no error in refusing to permit the cross-examination on this subject to extend to prior times wholly disconnected with and unrelated to the events concerned with her testimony. The exact extent to which cross-examination respecting collateral matters may go rests almost entirely in the discretion of the trial court.

58 Am. Jur. Sec. 624

*Johnston v. Jones* 1 Black (U.S.) 210, 17 L ed. 117

Re Dolbeer, 149 Cal. 227, 86 P 695

*Shailer v. Bullock*, 78 Conn. 65, 61 A 65

Since from the nature of the case no fixed rule can be devised defining the right and limiting the extent of irrelevant inquiry this must be determined by circumstances attending the particular case on trial, and an appellate court will not interfere with the exercise of discretion by the trial court unless a clear abuse thereof appears.

58 Am. Jur. Sec. 624

*Cochran v. United States* 157 U.S. 286, 39 L ed. 704, 15 S. Ct. 628

*Johnston v. Jones*, Supra

*Birmingham So. R. Co. v. Lintner*, 141 Ala. 420, 38 So. 363, 109 Am. St. Rep. 40

(5) Appellant complains of the exclusion of evidence relating to the assault by appellant Meeks on

witness Hartness, and evidence of an alleged attempted suicide of Hartness, and in particular exclusion of testimony of Doris Peterson Pineda (Tr. Vol. IV, P 993) concerning the latter point. These events were not associated with nor related to any fact described by the witness, or conversations had with the defendant concerning any issue in the case, and the reasons for exclusions of these collateral facts are discussed under Issue Number II. The court is referred to that section for the arguemnt. Furthermore, it is a fundamental principle of law that the "capacity of a person to act as a witness"( quoting from Page 59 of appellant's brief) or in other words, competency of a witness to testify, because of "emotional and mental instability" or any other reason is for the Court to decide and not the jury. Thus the rights of the defendant were not prejudiced in this respect.

(6) Appellant complains that Government witness William E. Didelius invaded the province of the jury in being allowed to state that the clothes worn by deceased at the time of his death did not have any evidentiary significance. It is respectfully submitted that this was not prejudicial to appellant. The witness was questioned at length by appellant on cross examination as to the condition of victim's clothes, and the fact of an examination by the F.B.I. Laboratory. The laboratory tests were not the subject of direct examination up and until the cross examination. The effect of the witness' testimony was that the clothes did not prove to be of any significance from his investi-

tion of the case and results of the laboratory examination. Though objected to by appellant, he later brought out on re-cross examination the information on which the witness based his conclusion. (Tr. Vol. 1, p. 163 to 169, particularly p. 165-166).

It should be noted that the testimony of the witness (Tr. p. 901-909) was given in the absence of the jury during the argument on a motion for discovery made at the close of the Government's case, and related in particular as to whether the deceased clothes were in existence. (See Tr. Vol. IV, p. 892-909).

Then on cross examination of this witness, who appeared for the Government in rebuttal, counsel for appellant thoroughly examined him in the presence of the jury, as to the witness' opinion of the evidentiary value of victim's clothes, as well as the information in the F.B.I. Laboratory report. (Tr. Vol. VI, P. 1449 to 1452)

Appellant cannot complain of the fact that the Court asked Government witness L. W. Hines if, from his description of the nature of the glasses, the person for whom they were made had rather poor vision or unusually poor vision. (Tr. Vol. I, P. 199) The Court may ask witnesses, including witnesses for the Government, questions on matters material to the case.

*State v. Scott* (Supr. Crt. Mo.) 58 S.W. 2d 275,  
P. 281

*People v. Moore* (Supr. Crt. Mich.) 10 N.W.  
2d 296



To contend that it was error for the Court to state during the trial of the case "I think I know the law" (Tr. Vol I, P. 199) is absurd. There is no more suggestion in such a remark, that counsel for defense doesn't know the law, than there is in denying a motion or overruling an objection made by counsel.

Thus it is respectfully submitted that neither the witness (Didelius) nor the Court erroneously and to the prejudice of appellant, invaded the province of the jury, and there was no error in the Court saying it understood the law.

(7) No error was committed by the Trial Court in granting the Government's motion to strike the testimony of Steve Chutuk, a Government witness. (Tr. Vol. VII, p. 1506 to 1510). The record amply shows that Chutuk had never discussed the facts he was relating with the United States Attorney, or anyone else, and that the Government was surprised by the statements made by the witness. No requests were made to cross examine the witness, and appellant made no objection to the motion.

*Kuhn et al v. United States* (CCA-9) 24 F 2d 910, Reh. Den. 26 F 2d 463, Cer. Den. 278 U.S. 605 was a case in which the United States Attorney was surprised by a witness called for the Government. He attempted to impeach the witness, over objection, by examining the witness as to previous contradictory statements. The Court stated that the practice was improper, but

held it was not prejudicial, in view of the fact that after a recess the United States Attorney on his own motion consented that the objections be sustained and that all the testimony be withdrawn from the consideration of the jury, which was done and the jury properly admonished.

Speaking on the same subject, Justice Hutcheson, in *Young v. United States* (CCA-5) 97 F 2d 200, Reh. Den. 97 F 2d 1023, a case in which the prosecution was surprised by the witness called for the Government, stated " . . . . *it is ordinarily the best practice*, if it can be effectively done, when a party shows that he has been surprised by the adverse testimony of a witness he has offered, to permit him to withdraw the witness and his testimony from the jury by having the whole evidence stricken from the record, as was done in *Kuhn v. U. S.*, 9 Cir. 24 F 2d 910. By this course, if the claim of surprise is made, as indeed it should be, only for the legitimate purpose of removing the prejudice of the surprising testimony and not for the purpose of getting the contradictory statements before the jury for their effect upon it, the purpose of protecting the party, who offered him, from injury at the hands of the witness is accomplished without complicating the issues or confusing the jury." (emphasis added)

## CONCLUSION

No reversible error was committed by the Trial Court in this case. It was not improper for the Court

to permit the Prosecuting Attorney to question a Government witness on his examination in chief concerning witness' previous conviction especially where no objection was made and where on cross-examination defense attorneys examined witness in detail as to type of crime, sentence and conditions relating thereto. Nor was it error for the Court to limit the cross-examination of Government witness Hartness as to the details of an entirely collateral offense where the fact of such collateral matter was permitted to be shown enabling the jury thereby to fully appraise the testimony of the witness. Since no affidavit was filed as required by Rule 17 (b) of the Federal Rules of Criminal Procedure no complaint can be made of the Court's denial to grant defendant's motion to summon certain defense witnesses and it is respectfully submitted that the defendant received a fair and impartial trial under the adversary theory of litigation.

The judgment of the Trial Court should, therefore, be affirmed.

Respectfully submitted,

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Assistant U. S. Attorney.





**In the United States**  
**CIRCUIT COURT OF APPEALS**  
**for the Ninth Circuit**

---

J. W. ROGERS,

*Appellant,*

vs.

PACIFIC ATLANTIC STEAMSHIP  
COMPANY, a corporation

*Appellee.*

---

**BRIEF OF APPELLEE**  
**PACIFIC ATLANTIC STEAMSHIP COMPANY**

---

Upon Appeal from the District Court of the United  
States for the District of Oregon.

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FILED

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## SUBJECT INDEX

	Page
Statement of the Case .....	1
Facts .....	3
Appellant's Assignments of Error .....	7
Appellant's Proposition I. ....	10
Appellant's Proposition II. ....	15
Appellee's Proposition I. ....	16
Conclusion .....	17

## TABLE OF CASES

	Page
Alvena, The, 22 Fed. 861 .....	9
Amazon, The, 144 Fed. 153 .....	16
Buckanan, The, 24 F. 2d. 528 .....	13
Brink v. Lyons, 18 Fed. 605 .....	13
Catalina, The, 95 F. 2d. 283 .....	16
City of Norwich, 279 Fed. 687 .....	7, 12
Collie v. Ferguson, 281 U.S. 52 .....	15
Cripple Creek, The, 52 F. Supp. 710 .....	13
Flynn v. Waterman Steamship Co., 44 F. Supp. 50 ....	7
Golden Sun, The, 30 F. Supp. 354 .....	13
Johnson v. Blanchard, 7 Fed. 597 .....	13
M. S. Elliott, 277 Fed. 800 .....	7
McCrea v. United States, 294 U. S. 23 .....	15
McKinnon v. The Reed, 39 Fed. 624 .....	13
O'Hara v. Luckenbach S.S. Co., 16 F. 2d. 681 .....	15
Port. Tug & Barge Co. v. Upper Col. Riv. Towing Co., 153 F. 2d. 237 .....	16
Puratich v. United States, 126 F. 2d. 914 .....	16
Silver Shell, The, 255 Fed. 340 .....	16
Steele v. Thacher, Fed. Cas. No. 13,348 .....	10
Stetson v. United States, 155 F. 2d. 359 .....	7
United States v. Wilhite, 163 F. 2d. 825 .....	17
18 U.S.C.A. §469 .....	12
46 U.S.C.A. §596 .....	15
46 U.S.C.A. §685 .....	11
46 U.S.C.A. §701 .....	10, 11



**In the United States**  
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Upon Appeal from the District Court of the United  
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---

**STATEMENT OF CASE**

This is an action wherein the libellant seeks recovery for the results of an alleged wrongful discharge. Libellant claims the wages he would have earned on the balance of the voyage and damages for "inconvenience, humiliation and anxiety."

The SS JEFFERSON MEYERS, upon which libelant was serving as First Assistant Engineer, commenced the voyage in question on January 7, 1946, bound for the Orient. The ship went to Shanghai, to the Phillipine Islands, and then back to Shanghai where, on June 19, 1946, the events took place which resulted in this law suit. In the afternoon of that day the master and libelant exchanged heated words as a result of which libelant went ashore, never to report for duty aboard this vessel again.

Libelant claims that he was discharged by the master on that day and that, because of the threats which the Master made against him, he was afraid of violence if he returned to the ship. Libelant was ordered to return to the ship by the United States Coast Guard office in Shanghai, but he refused to do so. He stowed away on the SS GENERAL MIX which left Shanghai while the JEFFERSON MEYERS was still in that port.

When the JEFFERSON MEYERS sailed from Shanghai on July 11, 1946, libelant was not aboard and was logged as a deserter. Upon the arrival of the ship at Seattle, Washington, the first continental United States port, the master turned libelant's wages earned through July 11, 1946, and his clothing over to the United States Shipping Commissioner for deposit with the District Court sitting in that city.

This proceeding has nothing to do with the wages earned on this voyage through July 11th. So far as the

record in this case shows and so far as counsel for appellee are informed, these wages are still on deposit with the Court.

Thus, the main issue presented to the trial court was whether libelant was wrongfully discharged or whether libelant was a deserter. The trial court found that there was no wrongful discharge and dismissed the case. In its opinion, the trial court stated (Ap 10):

“No doubt, in the light of all the unpleasantness that arose, Rogers felt justified in pursuing the course he took. Still, his conduct cannot now be condoned to the extent of allowing compensation for a job he failed and refused to carry through.”

## **THE FACTS**

During this entire voyage the JEFFERSON MEYERS was under the direction of the United States Government, military and civil. It took a cargo of wheat to China. Then it went to the Philippine Islands where a cargo, generally described as filthy and rotten, a cargo of surplus supplies being shipped for UNNRA in China, was loaded. In addition some dynamite was also put aboard. The ship returned to Shanghai.

Upon arrival at Shanghai it was found that the port was crowded. Under conditions of extreme heat, with filthy cargo and dynamite in her holds, the JEFFERSON MEYERS was required to stand off the Port of Shanghai for 14 days. (T. 113). No shore leave was granted during this period (T. 114). The food had been short and sometimes poor. On June 19, 1946, the nerves

and patience of all on the ship were taut to the point of breaking.

During the dinner hour on that day, some of the officers were entertaining a visitor, one Welch, at dinner aboard the ship. Captain Hughes came down for his evening meal and discovered the visitor eating at the deck officer's table, leaving no room for the master to eat. It was also against the rules for guests to be eating aboard without the prior approval of the master or the War Shipping Administration, charterer of the vessel. (T. 132). Whereupon, Captain Hughes ordered Welch off the ship.

Instead of leaving, Mr. Rogers, libelant, took Welch to his room. Captain Hughes, seeing this, went to Rogers' room and repeated his order that Welch leave the ship. (T. 119).

Soon thereafter Rogers and Welch went to the dock, and in plain view of the bridge of the JEFFERSON MEYERS, Rogers began writing a letter to the appellee, its agent in Shanghai, the American Consul, the Coast Guard and the War Shipping Administration, complaining of the master's conduct. (T. 16, 17). Rogers gave the Master a copy of the letter and told him what he was going to do with it. (T. 21).

*The foregoing events and conversations were the only occurrences between Rogers and the Master. There is absolutely no testimony that the Master told Rogers he was discharged or made any threats to Rogers.*



Libelant relies upon considerable hearsay testimony consisting of statements which the Master allegedly made to the Chief Mate and the Chief Engineer that Rogers was discharged and that Rogers would suffer severe injury if the Master saw him aboard the ship the next day.

In response to the charges filed by Rogers, the American Consul, acting through the United States Coast Guard, conducted a hearing aboard the ship. The investigating officer listened to the testimony of all parties involved as well as other officers and men aboard the ship. He concluded that the charges were not well founded and entered in the ship's official log book (Ex. 4):

"10 July 1946. Shanghai, China.  
Trouble aboard vessel settled by agreement. Master admonished. Charges against Master, Chief Mate and 1st Assistant Engineer withdrawn.

J. O. Thompson, Lt. Comdr.,  
U. S. C. G. R."

Attached to the official log is the report of the investigation by the Coast Guard to the American Consul in Shanghai, dated June 26, 1946, in which the officer reported:

"As a result of this investigation the master A. P. Hughes was admonished; chief mate, Robert W. Reusswig and acting first assistant J. W. Rogers, were ordered to return to the vessel and resume their regular duties.

"Reusswig and Rogers were warned that failure to comply with this order would result in a charge of desertion against them with a possible revocation of their license and the penalty of forfeiture as provided by law."

Both men refused to return to the ship unless the Coast Guard would give them orders in writing directing them to do so (T. 24). Such orders were given to Chief Mate Reusswig, he returned to duty, and continued the remainder of the voyage. He was not logged for the days he was ashore pending the settlement of these differences. He was paid for the three weeks when he was ashore and when he was not working aboard the ship.

Libelant Rogers avoided the service of the written order on him (T. 129), and in fact, stowed away on a vessel returning to the United States *six days before the JEFFERSON MEYERS sailed from Shanghai*. (T. 28, 46). The plain fact is that he never intended to return to the JEFFERSON MEYERS irregardless of the action taken by the Coast Guard and the American Consul.

It is to be noted that Chief Mate Reusswig was the person who claimed to have been actually threatened by the Master. He was the one who had all the direct contact with the Master. Yet he followed the lawful directions of the proper authorities. He returned to the ship and completed the voyage. He received all his pay for the remainder of the voyage and he suffered no "inconvenience, humiliation and anxiety."

The trial court heard all the testimony and observed the witnesses. There was no testimony by deposition. He concluded that Rogers *did not* flee because he feared the Master. "Their differences reached no higher level than a school-yard quarrel."

## **APPELLANT'S ASSIGNMENTS OF ERROR**

In his brief appellant does not mention his assignments of error. These errors, while assigned, are not argued and they should, therefore, be deemed waived. *Stetson v. United States*, 155 F. 2d. 359 and cases cited therein.

Appellant does spend considerable time and space in his brief arguing the facts. In reality his Assignments of Error are only allegations that the trial court found the facts against appellant. Most of the evidence is conflicting, as the Court will determine upon examination of the record herein.

The evidence does not show, as appellant claims, that Rogers was discharged. It does show that Rogers deserted the ship.

Desertion consists in the abandonment of duty by quitting the ship before the termination of the engagement, without justification, and with the intention of not returning. *City of Norwich*, 279 Fed. 687; *M. S. Elliott*, 277 Fed. 800; *Flynn v. Waterman Steamship Company*, 44 F. Supp. 50.

The evidence is abundant that Rogers never intended to return to the ship. He was dissatisfied with the results of the Coast Guard hearing and the action of the American Consul to such extent that he inspired inflammatory propaganda similar to that in Exhibit 2. (T. 43). He was seeking support "for pressing these charges and having

the guts to carry it to the Admiralty Court over the actions of the U. S. Consul and the Coast Guard Hearing Detail."

Rogers refused to accept the oral order of the Coast Guard officer that he return to the ship. (T. 24). He deliberately absented himself so that a written order could not be given him. (T. 129). He even stowed away on another vessel six days before the JEFFERSON MEYERS sailed. (T. 28, 46). Such a course of conduct makes it clear that Rogers never intended to return to this ship.

In view of all the circumstances at the time, Rogers had no justification for leaving the ship. There was no direct threat ever made to Rogers. It was all hearsay to him. The Chief Engineer told him some, the Chief Mate told him something else. There was no previous trouble between Rogers and the Master; in fact, they were pictured as great friends all through the voyage up until June 19. (T. 36, 111). There was no evidence of any violence on the part of the Master either before, during or after the Shanghai incident. Attempt has been made to taint the Master by showing allegedly arbitrary and unreasonable acts before and after the Shanghai incident, but in not one of these acts is any violence shown.

How then can Rogers justify his leaving the JEFFERSON MEYERS on the grounds of fear? All he had was a hearsay threat from a person he had always been able to get along with and with whom he was very friendly.



The testimony concerning the Master's conduct on June 19th is conflicting. Rogers' story is colored by his wounded pride. Such does not constitute a justification for desertion. *The Alvena*, 22 Fed. 861.

The claims of drunkenness, threats of great bodily harm, discharges, etc., were all denied by the Master. The testimony shows that the Master was armed, but he was so armed because of the belligerent attitude of some of the crew, including Rogers (T. 124). The Master made no threat to Rogers.

The occurrences respecting Welch in the dining saloon are greatly magnified and distorted in Rogers' testimony and contradicted by the Master.

One of the chief complaints made by Rogers was that the Master was required to report to the Chinese Customs all unmanifested articles. (T. 127). Upon inspection by the Chinese Customs many contraband articles were found, including a jeep Rogers had obtained (T. 45). Resentment against the Master because of this was probably one of Rogers' most impelling motives in pursuing his course of conduct.

In his opinion the trial court stated that the evidence did "not compel conviction that plaintiff fled because he feared the Master. Their differences reached no higher level than a school-yard quarrel." (Ap. 10). The trial court also made the following finding of fact (Ap. 12):

### III

"Plaintiff deserted said ship because of petty differences with the Master and such desertion was not caused by fear or threats from the Master as claimed by plaintiff."

**APPELLANT'S PROPOSITION I**

Appellant contends as a matter of law that a seaman is justified in leaving a vessel through fear induced by cruel treatment and threats of physical violence. After stating this principle of law, appellant argues the evidence from pages 9 through 29 of his brief.

First as to the proposition of law. The majority of the decided cases upon this proposition are cases where the seaman is seeking recovery of wages he earned before he left the ship. If the seaman deserted, he would not be entitled to those earned wages. 46 U. S. C. A. §701.

Generally the courts hold that unreasonable and continued acts of cruelty by the officers of a ship will justify a seaman leaving the ship. But such cruelty and oppression must be grossly excessive.

*Steele v. Thacher*, Fed. Cas. No. 13,348:

“There may be cases of such extreme and per-severing cruelty on the part of the master as will justify him in deserting. But it must be a strong case. I am, as at present advised, far from being prepared to hold that a battery, simply because it is excessive, will be a justification, even though it should pass very considerably beyond the limits of a moderate discretion. As a general rule, it seems to me that another ingredient should enter into the case. The seaman who proposes, on this ground to justify a desertion, should not only exhibit proof of the injury, but a just and reasonable ground of apprehension that it would be causelessly repeated, either by showing a general disposition to cruelty on the part of the master, or the existence of some particular pique or mal-

evolence toward him personally. The policy of the law discourages the separation of the mariner from the vessel before the termination of the voyage, especially in a foreign port."

The Steele case is one of the early cases on the duty of seamen to remain with the ship and states law which is good today. The statutes look with disfavor on a man leaving a ship before the termination of the voyage. 46 U. S. C. A. §701.

Congress has provided the machinery to settle problems, such as arose here, at the time they arise. Under 46 U. S. C. A. §685, the American Consul must inquire into any complaints made by seamen that the vessel is unseaworthy or against the officers for cruel treatment. If he finds the charges to be true, he orders that the seamen be paid an additional month's wages and provided with employment on another ship or transportation home.

Rogers, being a seaman fully aware of all his rights, immediately brought his charges against the Master before the American Consul. (T. 17). In accordance with the statute, the Consul instituted an inquiry into the matter and decided against the charges. (Ex. 4). Mr. Reusswig, the Chief Mate, recognized the powers and responsibilities of the Consul and, when the order was given to return to the ship, did so. Although he may have resented the decision against him, he knew that by law he was required to return. (T. 77).

Rogers, however, would not accept the decision of the Coast Guard and American Consul. He took the law

into his own hands and refused to obey the orders to return to his ship. He violated the statute against stowing away on vessels, 18 U. S. C. A. §469, by returning home on the GENERAL MIX. Other employment was available to him through the War Shipping Administration in Shanghai, but Rogers was too anxious to institute a law suit to seek his vengeance on the Master to sign off the JEFFERSON MEYERS. (T. 28). He could have been gainfully employed as an engineering officer during the period for which he now seeks recovery, but he failed to do so and thus failed to minimize his loss.

Under these circumstances, it appears that Rogers was properly classed in the log book and on the Shipping Articles as a deserter (Ex. 3).

*The City of Norwich*, 279 Fed. 687, discussed in appellant's brief, is not in point in this case. The libellants in the *City of Norwich* were claiming wages up to the time they left the ship. They were attempting to avoid the forfeiture of these wages by asserting cruelty on the part of the ship's officers. As pointed out previously in this brief, appellant is not suing here to recover for the wages earned up to the time he left the ship. These are on deposit in the District Court sitting in Seattle.

If Rogers was not a technical deserter from the JEFFERSON MEYERS, he would be entitled to his wages up to the time he left the ship. A seaman who absents himself without leave and does not return to the ship by sailing time, under circumstances not amounting to



desertion, may recover the amount of his wages actually earned but is not entitled to wages for the balance of the voyage covered by the Shipping Articles. *Johnson v. Blanchard*, 7 Fed. 597; *Brink v. Lyons*, 18 Fed. 605; *McKinnon v. The Reed*, 39 Fed. 624; *The Buckanan*, 24 F. 2d. 528. See also *The Cripple Creek*, 52 F. Supp. 710.

Appellant makes some contention concerning his alleged "discharge" by the Master. Appelle contends that there is no evidence that the Master did discharge Rogers, and, under the law, the Master could not discharge Rogers without the consent of the American Consul. Judge Yankwitch clearly summarizes the protection given seamen in the matter of discharges in foreign ports in *The Golden Sun*, 30 F. Supp. 354, where he says:

"The provision calling for the intervention of an American Consul in discharging a seaman in a foreign port, U. S. Rev. Stats, Sec. 4580, 46 U. S. C. A. §682, is very old in our law. The first enactment dates back to the act of February 28, 1851, 2 Stats. 203; See: *Tingle v. Tucker*, 1849, Fed. Cas. No. 14,057. It was made more for the benefit of the seamen, than of the owners of a ship. It seeks to protect them against arbitrary discharge or discharge for causes not warranted by the practices under maritime law. Since its enactment, it has been determined definitely that the intervention of the Consul is a condition precedent to a valid discharge. The master who, without seeking such intervention, discharges a seaman, runs the risk of having to prove the justness of the discharge. As said by Attorney-General Caleb Cushing: 'He (the master) had no right to determine of himself the facts on which he assumed to act, nor to consummate the discharge without intervention of the consul.' Discharge of Seamen, 7 Op. Atty. Gen. 1855, p. 349, 350.

“And see: *Hathaway v. Jones*, D. C. Mass. 1863, Fed. Cas. No. 6212; Discharge of Seamen in Foreign Port, 16 Op. Atty. Gen. 1879, page 268; *Nieto v. Clark*, 1858, D. C. Mass., Fed. Cas. No. 10,262; *The Annie*, D. C. N. Y., 1904, 133 F. 325; *Mattes v. Standard Transportation Co.*, D. C. N. Y. 1921, 274 F. 1019, 1023.”

In the present case there is no direct testimony by Rogers that he was discharged by the Master. There is only hearsay testimony to Rogers in which he states that the chief engineer informed him that the Master wished to discharge Rogers and also the testimony of Mr. Reusswig. The entry in the engine log, upon which appellant places reliance, clearly shows that Rogers did not accept the chief engineer's statement that he was discharged. The entry shows (Ex. 1): “Mr. Rogers gone to Consul, ordered off the ship by Captain, his time to terminate this date at midnight.”

This entry shows that Rogers did not except the alleged discharge and knew where he should go to get relief.

It is clear that Rogers was not discharged and that he did not consider himself discharged.

He was not afraid of the Master. He merely left the ship because of petty differences with the Master and not because of fear or threats from the Master. He is not entitled to a finding that he should have his wages and damages for the indignities and inconveniences he suffered because such were caused solely by his own conduct.

## APPELLANT'S PROPOSITION II

Rogers did not claim double wages under R. S. 4529, 46 U. S. C. A. §596, at the time of trial. This is being raised for the first time on this appeal.

This section provides that "Every Master or owner who refuses or neglects to make payment . . . . without sufficient cause shall pay to the seaman a sum equal to two days' pay for each and every day during which payment is delayed beyond the respective periods."

The words "refuses or neglects to make payment . . . . without sufficient cause" connote conduct which was arbitrary, unreasonable or willful. *Collie v. Ferguson*, 281 U. S. 52, 74 L. Ed. 696; *McCrea v. U. S.*, 294 U. S. 23, 79 L. Ed. 735.

Rogers is certainly not entitled to double wages for the money earned up through July 11, 1946, because the master could not have paid that money on that day. Rogers was homeward bound as a stowaway on the GENERAL MIX at that time. As soon as the ship touched a continental United States port, those wages were paid to the Shipping Commissioner.

Rogers also apparently claims that he should be paid double wages for those wages unearned by him for the remainder of the voyage after the ship left Shanghai. The cases are uniform that where there is a doubtful legal question of a seaman's right to wages, refusal to pay these wages does not subject the Master or owner to the penalty of double wages. *O'Hara v. Luckenbach*

SS Co., 16 F. 2d. 681; *The Silver Shell*, 255 Fed. 340; *The Amazon*, 144 Fed. 153.

Rogers' claim for double wages under R. S. 4529 is without merit.

### APPELLEE'S PROPOSITION I

Where the trial judge saw the witnesses, heard their testimony, and had an opportunity of passing upon their credibility and accuracy, his findings of fact and conclusions of law should not be disturbed.

This is a familiar proposition of law which requires little citation and is peculiarly applicable to this appeal. While an admiralty appeal is a trial de novo, the presumption in favor of the findings of the District Court is at its strongest. *The Catalina*, 95 F. 2d. 283; *Puratich v. United States*, 126 F. 2d. 914; *Portland Tug & Barge Co. v. Upper Columbia River Towing Co.*, 153 F. 2d. 237.

When questions of fact are dependent upon conflicting evidence, the decision of the trial judge who had the opportunity of seeing the witnesses and judging their appearance, manner and credibility, should not be reversed. Here the trial court saw and heard all the witnesses. There was no testimony by deposition. He resolved the conflicting testimony and decided that Rogers did not flee "because he feared the Master. Their differences reached no higher level than a school-yard quarrel." In view of the conflicting testimony and with the weight of the evidence being in favor of the appellee,



the trial court should be sustained.

See also *United States v. Wilhite*, (CCA 9, 1947) 163 F. 2d. 825.

### CONCLUSION

Appellee respectfully urges that the judgment and decree of the District Court be affirmed. The evidence is ample and satisfactory that the appellant left the ship in Shanghai because of petty differences with the master. He was not in fear of the master. His disregard of the lawful authority of the American Consul and of the laws regarding stowaways disqualify him from any sympathetic treatment by a court of law. The trial court was right. It should be affirmed.

Respectfully submitted,

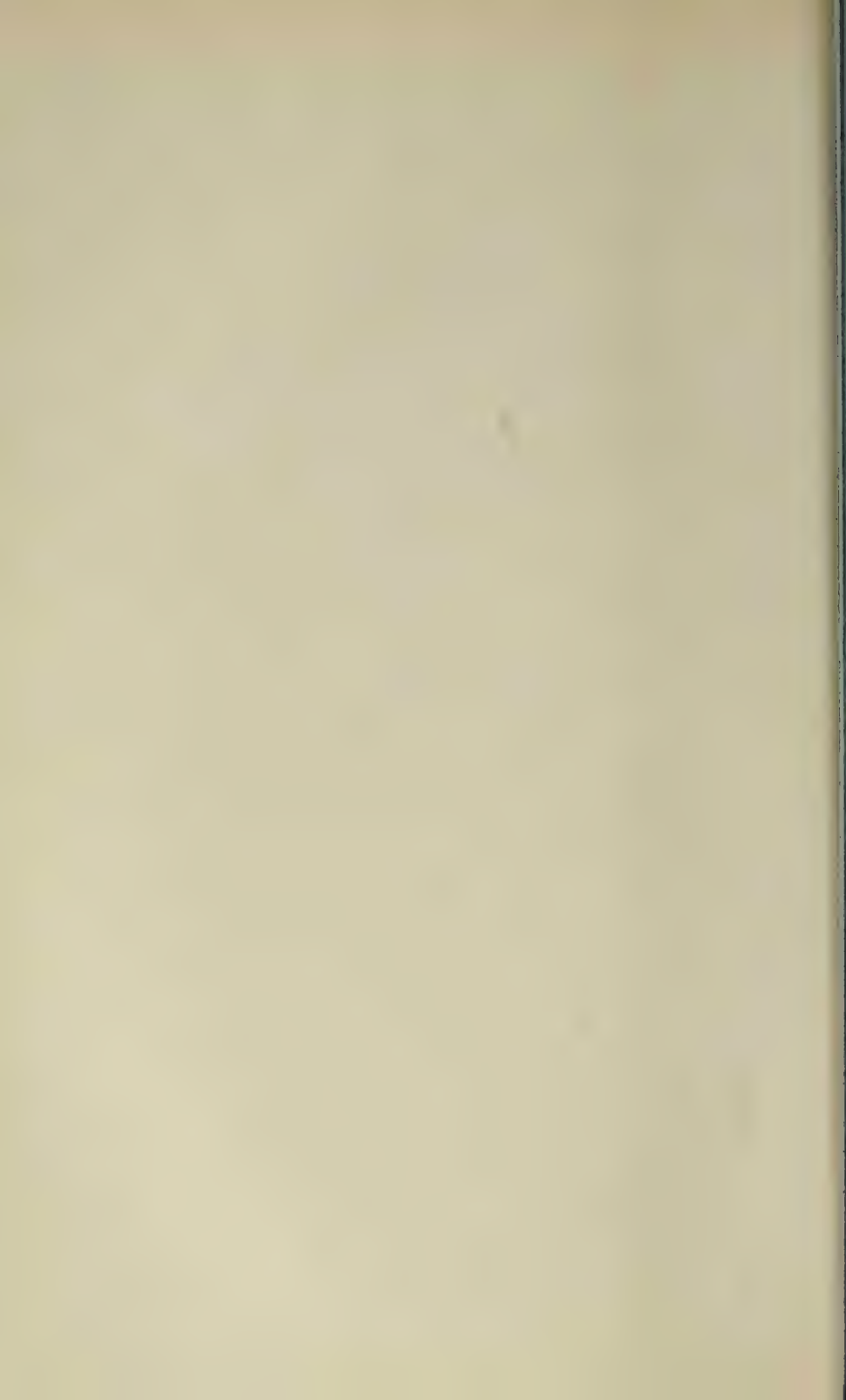
WOOD, MATTHIESSEN & WOOD,

LOFTON L. TATUM,

1310 Yeon Building,

Portland 4, Oregon,

*Proctors for Appellee.*



No. 11917

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United States  
Circuit Court of Appeals  
For the Ninth Circuit.

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GEORGE H. RICHARDSON,  
Appellant,  
vs.

THE TRAVELERS INSURANCE COMPANY,  
Appellee.

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Transcript of Record

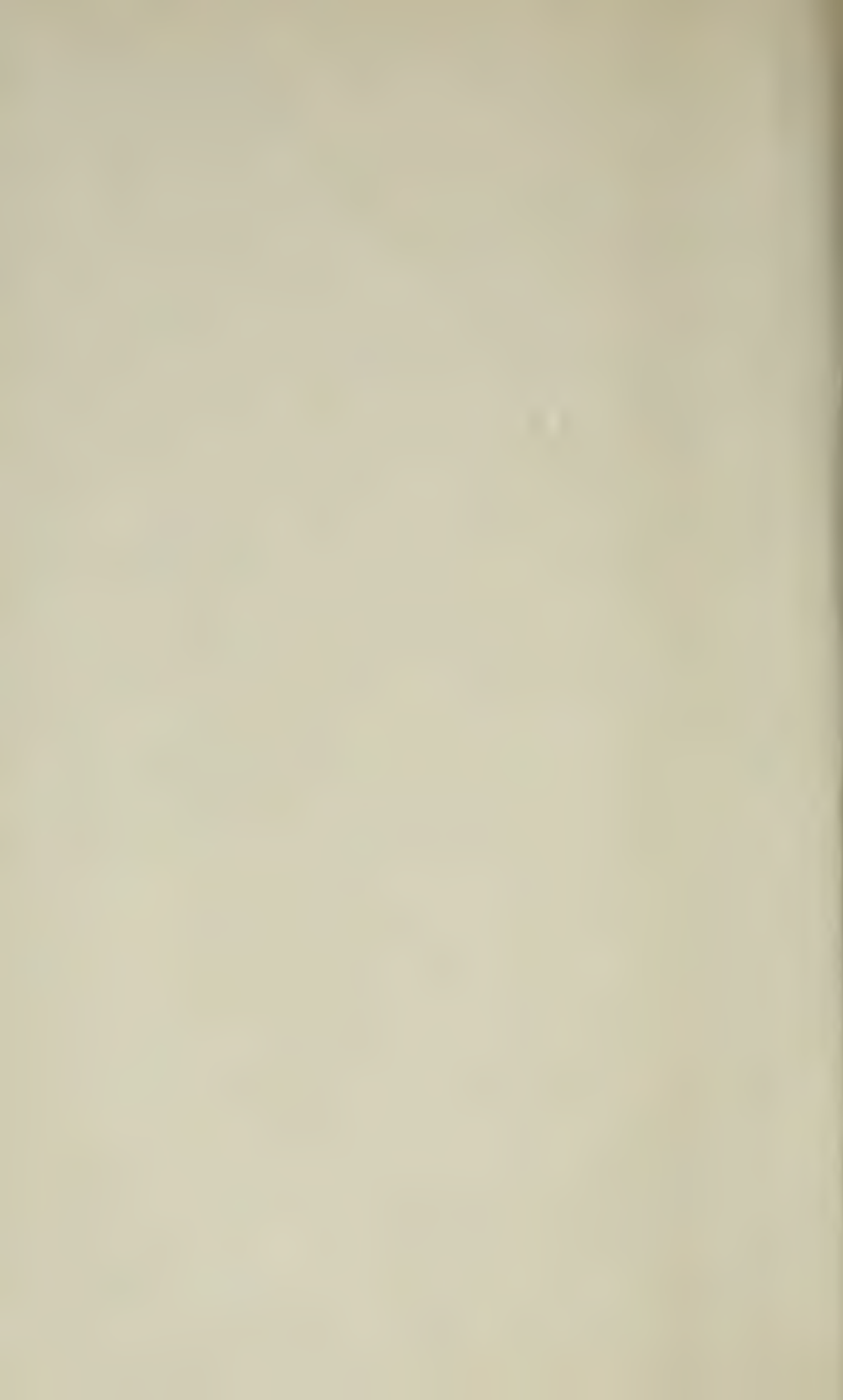
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Upon Appeals from the District Court of the United States  
for the Northern District of California,  
Southern Division

FILED

JUL 15 1948

PAUL P. O'BRIEN,  
CLERK









No. 11917

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United States

Circuit Court of Appeals

For the Ninth Circuit.

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GEORGE H. RICHARDSON,

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## INDEX

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

	PAGE
Answer and Counterclaim.....	21
Exhibit No. 1—Policy Issued 12/31/26....	31
Answer to Counterclaim.....	37
Appeal:	
Certificate of Clerk to Transcript of Record on.....	75
Designation (DC) of Contents of Record on.....	73
Notice of.....	70
Statement of Points and Designation of Record (CCA) on.....	132
Statement of Points (DC) on Which Appellant Intends to Rely on.....	71
Certificate of Clerk to Transcript of Record on Appeal .....	75
Complaint for Reformation of Insurance Policy .....	2
Exhibit A—Application for Insurance Annuity .....	5
B—Insurance Policy.....	7
C—Insurance Policy (applied for) .....	14

INDEX	PAGE
Designation (DC) of Contents of Record on Appeal .....	73
Findings of Fact and Conclusions of Law.....	50
Conclusions of Law.....	63
Findings of Fact.....	51
Judgment .....	66
Names and Addresses of Attorneys.....	1
Notice of Appeal.....	70
Opinion and Order.....	41
Reporter's Transcript.....	76
Witness for Defendant:	
Richardson, George H.	
—direct .....	113
—cross .....	97, 124
Witnesses for Plaintiff:	
Waterman, Harold A.	
—direct .....	78
—cross .....	84
—redirect .....	87, 89
—recross .....	88
Weightman, James A.	
—direct .....	90
—cross .....	95

## INDEX

## PAGE

## Witnesses for Plaintiff—(Continued):

Whitaker, Gerald

—direct .....105, 129

—cross .....110, 129

—redirect ..... 130

## Statement of Points (DC) on Which Appellant

Intends to Rely on Appeal..... 71

## Statement of Points on Which Appellant In-

tends to Rely on Appeal and Designation of

Parts of Record Appellant Thinks Nec-  
essary for Consideration Thereof (Rule 19,

Subd. 6-CCA-9th)..... 132





NAMES AND ADDRESSES OF ATTORNEYS

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San Francisco,

Attorneys for Appellee.

In the United States District Court, in and for  
the Northern District of California, Southern  
Division

No.....

THE TRAVELERS INSURANCE COMPANY,  
Plaintiff,

vs.

GEORGE H. RICHARDSON,  
Defendant.

COMPLAINT FOR REFORMATION OF  
INSURANCE POLICY

Plaintiff complains of defendant and for cause  
of action alleges as follows:

I.

That at all times herein mentioned plaintiff has  
been and now is a corporation duly organized and  
existing under and by virtue of the laws of the  
State of Connecticut, and duly authorized to trans-  
act the business of life insurance in the State of  
California; that plaintiff is a citizen of the State  
of Connecticut; that defendant is a citizen of the  
State of California; that the matter in contro-  
versy exceeds, exclusive of interest and costs, the  
sum of \$3,000.00.

II.

That heretofore, to wit, on the 13th day of De-  
cember, 1926, defendant applied to plaintiff that  
there be issued to defendant an insurance annuity

in the amount of \$10,000.00 on the uniform [1\*] premium plan; that a copy of said application is attached hereto, marked Exhibit "A," and made a part hereof.

III.

That thereafter and on the 3rd day of January, 1927, pursuant to said application, plaintiff made, issued, executed and delivered to defendant its certain policy of insurance, a copy of which is attached hereto, marked Exhibit "B," and made a part hereof.

IV.

That by mutual mistake said policy of insurance so issued to defendant was not the policy of insurance applied for by defendant, nor the policy intended to be issued by plaintiff.

V.

That a copy of the policy of insurance applied for by the defendant is attached hereto, marked Exhibit "C," and made a part hereof.

VI.

That plaintiff does not keep any copies of policies issued by it to its assureds and did not keep any copies of the policy issued by it to defendant, and nothing in plaintiff's records would disclose the mistake in furnishing the wrong policy form to defendant; that plaintiff's first knowledge of said mistake was in the month of March, 1946, when

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\*Page numbering appearing at foot of page of original certified Transcript of Record.

said policy of insurance became the subject of discussion between plaintiff and the assignee of said policy of insurance, The Crocker First National Bank of San Francisco.

As and for a separate and distinct cause of action, plaintiff complains of defendant and alleges as follows:

### I.

Special reference is hereby made to the allegations of paragraphs I, II, III, V and VI of the first cause of action hereinabove set forth and by this reference each and all of the allegations thereof are incorporated in and made a part of this second cause of action [2] with like force and effect as if fully set forth herein.

### II.

That by mistake of plaintiff which defendant at the time knew or suspected, said policy of insurance so issued did not truly express the intention of the parties thereto in this that said policy was not the policy of insurance applied for by defendant, nor the policy intended to be issued by plaintiff.

Wherefore, plaintiff demands judgment that said policy of insurance so issued to defendant be reformed and corrected so as to state and provide in the Special Privileges Section thereof for each \$1,000.00 of insurance that the second option upon surrender of the policy the insured may receive a cash payment of \$395.00 and a paid up contract, payable at death, for \$1,000.00 in lieu of a cash



payment of \$739.00 and a paid up contract, payable at death, for each \$500.00 of insurance; and that defendant surrender and deliver the said policy of insurance to the plaintiff so that the same may be written and corrected accordingly, and for such other and further relief as to the Court may seem meet and proper in the premises.

JOSEPH T. O'CONNOR,

HAROLD H. COHN,

Attorneys for Plaintiff. [3]

EXHIBIT "A"

The Travelers Insurance Company

Hartford, Connecticut

The Undersigned (Insured, Beneficiary and Assignee if any) hereby request that in lieu of Contract No. 373735 - 482573 upon the life of George H. Richardson there be issued a new contract as follows:

1. Amount, \$10,000.00; Form Ins. Annuity Age 65 on the Uniform Premium Plan with No A Disability Provision
2. A. Premiums Payable annually.  
B. Date of Birth: Month, Aug.; Day, 21;  
Year, 1881  
C. Date of Policy: 9-27-16  
D. Ratable age: 35
3. Beneficiary: Alice L. Richardson, Wife
4. Special instructions: Contingent Beneficiary: Wendell L. Richardson, son, and Mary L. Richardson, daughter, equal shares, or in case of their death to their children, if any, in equal shares.

In consideration of issue of the new contract and effective upon delivery thereof, the aforesaid original contract is hereby released and surrendered to The Travelers Insurance Company, Hartford, Connecticut, together with all right, title, claim, interest and benefit which the Undersigned have or may have thereunder; and the undersigned do hereby certify and declare that no person, firm or corporation other than those joining in this release have any interest or right therein or any title, legal or equitable, in whole or in part thereto.

/s/ GEORGE H. RICHARDSON,

Insured,

-----,

Beneficiary,

-----,

Assignee.

Dated at San Francisco, Calif., December 13,  
1926. [4]

District Court of the United States for the Northern  
District of California, Southern Division

No. 26322-S

THE TRAVELERS INSURANCE COMPANY,  
Plaintiff,

vs.

GEORGE H. RICHARDSON,  
Defendant.

### ANSWER AND COUNTERCLAIM

Comes now the defendant George H. Richardson and in answer to plaintiff's complaint admits, denies and alleges as follows:

#### I.

Admits the allegations of Paragraph I of said complaint.

#### II.

Except as herein otherwise admitted, denies the allegations of Paragraph II of said complaint but alleges that on September 27th, 1916, the plaintiff sold defendant its life insurance policy No. 373,735 in the amount of \$15,000, which policy provided for annual premiums in the amount of \$309.75.

That on December 13, 1918, the plaintiff also sold defendant its life insurance policy No. 482573 in the amount of \$10,000.

That on or about December 13, 1926, the plaintiff prevailed [8] upon defendant to convert said above numbered policies, aggregating \$25,000 of life in-

surance into its policy, also numbered 373,735, and thereafter issued said policy to defendant, a photostatic copy of which said policy, dated December 31, 1926, and effective September 27, 1916, is attached hereto, marked Exhibit "1" and expressly made a part of this answer and counterclaim.

### III.

Save and except as herein otherwise admitted, denies the allegations of Paragraph III of plaintiff's complaint.

### IV.

Denies the allegation of Paragraph IV of the complaint.

### V.

Denies the allegations of Paragraph V of the complaint

### VI.

Denies the allegations of Paragraph VI of the complaint, but alleges, in this respect, that the plaintiff, The Travelers Insurance Company, knew, as early as the year 1927 that said policy was issued as set forth in defendant's Exhibit "1" hereto attached.

As and for an answer to plaintiff's separate and second cause of action, defendant denies, admits and alleges as follows:

### I.

Denies the allegations of Paragraph I of said second cause of action, save and except the same may be admitted as alleged in the answer herein to plaintiff's first cause of action.



II.

Denies the allegations of Paragraph II of said second cause of action. [9]

As and for a separate and distinct answer to plaintiff's said causes of action, this defendant alleges:

I.

That the plaintiff insurer is guilty of laches in the premises as follows:

- a. That at the time defendant insured converted his said policies No. 373,735 and No. 482,573, he then had a loan on said Policy No. 373,735 with the plaintiff insurer; that during the month of July, 1928, this defendant delivered said Policy No. 373,735 into the hands of the plaintiff insurer for the purpose of negotiating a further loan thereon; that said plaintiff insurer had said policy in its possession and did not return the same to this defendant insured until some time during the month of August, 1928.
- b. That during 1931, this defendant insured again negotiated a loan on his said Policy No. 373,735 and on or about the month of September 1931 delivered his said Policy No. 373,735 to the said plaintiff insurer; that while said policy loan was being negotiated, the plaintiff insurer had said policy in its possession and did not return it to this defendant insured until some time during the month of October 1931.

- c. That during 1933, this defendant insured again negotiated a further loan on his said Policy No. 373,735, and on or about the month of October 1933 delivered his said policy into the hands of said plaintiff insurer; that while said policy loan was being negotiated, the plaintiff insurer had said policy in its possession and did not return it to this defendant insured until some time during the month of November 1933. [10]
- d. That during the year 1936, this defendant insured again negotiated a further loan on his said Policy No. 373,735 and on or about the month of June, 1936, delivered his said policy to the said plaintiff insurer; that while said policy loan was being negotiated, the plaintiff insurer had said policy in its possession and did not return it to this defendant insured until some time during the latter part of the month of June 1936.
- e. That by reason of said loans, the plaintiff insured, The Travelers Insurance Company, well and truly knew, as early as the years 1926, 1928, 1931, 1933 and 1936, that said Policy No. 373,735, including the "Special Privileges" provisions thereof, was in the exact form set forth in defendant's Exhibit "1" attached hereto.

That the premiums on said Policy No. 373,735 for \$15,000, dated September 27, 1916, were \$309.75 per annum, while the premiums on said Policy No.

373,735, dated December 31, 1926, for \$10,000 were \$287.50 per annum. That the higher rate charged by the plaintiff for said 1926 policy was principally on account of the special privileges contained in said policy, including Option 1 under "Options Available at Age 65" shown on Page 2 of [11] said policy (Exhibit "1" attached hereto).

- f. That the said plaintiff, although knowing or suspecting or by the exercise of reasonable care and/or diligence and/or prudence should and/or would have known of the exact provisions of said policy, nevertheless remained silent and waited for a period of twenty years and until this defendant had faithfully kept and performed all the terms and conditions of said contract on his part to be performed, including the collection by the plaintiff insurer from the defendant of all twenty of said annual premiums called for in said 1926 policy, before bringing this suit.
- g. That as a result of the acts of the plaintiff insurer The Travelers Insurance Company, in soliciting and importuning this defendant to drop and discontinue said 1918 life insurance policy No. 482,573 in the amount of \$10,000 and the conversion of said life insurance policy No. 373,735, dated September 27, 1916, in the amount of \$15,000 for said converted life insurance policy No. 373,735, dated December 31, 1926, in the amount of \$10,000 with special privileges, this defendant has been prejudiced in that he dropped and discontinued said prior life insurance policies aggregating \$25,000 for his said present policy in the amount of \$10,000 with Special Privileges.

As and for a second, separate and distinct defense to plaintiff insurer's first and second causes of action, this defendant alleges:

I.

That plaintiff insurer's first and second cause of action are outlawed and barred by the express provisions of the Statute of Limitations, to wit: Sections No. 312 and No. 338 of the Code of Civil Procedure, of the State of California, the applicable parts of which read as follows:

Sec. No. 312:

"Civil Actions. Civil actions, without exception, can only be commenced within the periods prescribed in this title, after the cause of action shall have accrued, unless where, in special cases, a different limitation is prescribed by statute." [12]

And Section No. 338:

"Three years—. . . Fraud and Mistake.

"Within Three years: . . . 4. An action for relief on the ground of fraud or mistake. The cause of action in such case not to be deemed to have accrued until the discovery, by the aggrieved party, of the facts constituting the fraud or mistake."

That the plaintiff insurer's present complaint now constitutes a stale and outlawed demand.

As and for a third, separate and distinct defense to plaintiff insurer's said first and second causes of action, this defendant alleges:



## I.

That by the express terms of said contract of insurance, the plaintiff insurer is debarred and prohibited from contesting said policy. That in this respect said policy provides in part as follows:

“Incontestability. This contract shall be incontestable after one year from date of issue, except for non-payment of premiums. It is free from conditions as to residence, occupation, travel or place of death. No permit or extra premium will be required for military or naval service in time of war or in time of peace.

“This contract is subject to the privileges and conditions recited on the subsequent pages hereof.”

As and for a counterclaim, defendant alleges:

## I.

That the plaintiff, The Travelers Insurance Company is now and at all of the times herein mentioned was, a corporation organized and existing under and by virtue of the laws of the State of Connecticut and duly qualified and licensed in so far as this action is concerned, to transact a general insurance business as a life, accident and health insurance company, by the Insurance Commissioner of the State of California; that defendant is a citizen of the State of California and that the matter in controversy exceeds, exclusive of interest and costs, the sum of \$3,000.

## II.

That heretofore, to wit, on or about the 31st day of December, 1926, [13] said plaintiff made and delivered to defendant its certain policy No. 373735, dated the 31st day of December, 1926, but effective from September 27, 1916, insuring the life of defendant, and after the payment by defendant of thirty (30) annual premiums and his attaining the age of sixty-five (65) years, said plaintiff promised and agreed in writing in said policy, among other things, to pay defendant as follows:

## “Special Privileges

Options Available at Age 65. The Insured may select in lieu of all other benefits hereunder one of the following options to become available upon the surrender of this contract at its anniversary when the Insured shall have reached the age of 65, the amount of these options being stated for each \$500 of insurance:

1. Receive a cash payment of \$1,083.00.
2. Receive a cash payment of \$739.00 and a paid-up contract payable at death for \$500.00.
3. Receive a paid-up contract payable at death for \$1,574.00.
4. Receive an annual income of \$112.83 payable during the natural life of the Insured.”

## III.

That a photostatic copy of said policy is attached hereto, marked Exhibit “1” and expressly made a part of this counterclaim.

## IV.

That under the provisions of said policy and the "Options Available at Age Sixty-five," provided in said policy, defendant has elected and does elect to receive a cash payment of Twenty-one Thousand Six Hundred Sixty Dollars (\$21,660.00) in full settlement of the amount due under said policy as provided in said "Special Options."

## V.

That under the express terms of said policy the plaintiff agreed to pay to defendant said sum of \$21,660.00. [14]

## VI.

That defendant, since said 27th day of September, 1916, has paid to plaintiff all of said thirty (30) annual premiums due under said policies No. 373-735, and has paid to plaintiff all sums and premiums called for in said policy and due from defendant to the plaintiff.

## VII.

That defendant attained the age of sixty-five (65) years on August 21st, 1946, and that by reason thereof said policy, according to the terms thereof, matured on September 27, 1946.

## VIII.

That, notwithstanding the fact that defendant has performed all of the terms and obligations of said contract on his part to be performed, said plaintiff has failed and refused and still fails and refuses to pay to defendant said sum of \$21,660.00.

Wherefore, defendant prays that plaintiff take nothing by its said action; that this defendant have judgment against said plaintiff for said sum of Twenty-one Thousand Six Hundred Sixty Dollars (\$21,660.00), plus interest from the 27th day of September, 1946; for costs of this action and for such other and further relief as to this Court may seem proper.

ALVIN GERLACK,

Attorney for Defendant. [15]

State of California,

City and County of San Francisco—ss.

George H. Richardson, being first duly sworn, deposes and says:

That he is the defendant in the above entitled action; that he has read the foregoing Answer and Counterclaim and knows the contents thereof; that the same is true of his own knowledge except as to the matters therein stated on information and belief and as to those matters that he believes it to be true.

GEORGE H. RICHARDSON

Subscribed and sworn to before me this 8th day of November, 1946.

[Seal]

ALFRED D. MARTIN,

Notary Public in and for the City and County of San Francisco, State of California.

[Endorsed]: Filed Nov. 8, 1946.







[Title of District Court and Cause.]

ANSWER TO COUNTERCLAIM

Now comes The Travelers Insurance Company, plaintiff in the above-entitled action, and files this its answer to defendant's counterclaim in said action and avers and denies as follows:

Admits the allegations of Paragraphs I, II, III, IV and V.

Admits the allegations of Paragraph VI but avers that the premiums specified as due on the policy of insurance issued to defendant were not proper premiums for said policy in this that said premiums were the proper premiums for a policy of insurance carrying with it the right to receive at age 65 for each \$1,000.00 of insurance a cash payment of \$395.00 and a paid up contract at death for \$1,000.00, but not the right to receive at age 65 a cash payment of \$739.00 for each \$500.00 of insurance and a paid up contract at death for \$500.00.

Admits the allegations of Paragraphs VII and VIII, but [17] avers that while the defendant has performed the terms and conditions indicated by mistake in the policy issued to him, he has not performed the terms and conditions omitted by mistake from said policy and has only performed the terms and conditions in the policy of insurance applied for by him.

As a further and separate answer and defense to said counterclaim, plaintiff alleges:

## I.

That heretofore, to wit: on the 13th day of December, 1926, defendant applied to plaintiff that there be issued to defendant an insurance annuity in the amount of \$10,000.00 on the uniform premium plan; that a copy of said application is attached to the Complaint on file in this action, marked Exhibit "A" and made a part thereof, and by this reference said application is made a part hereof.

## II.

That thereafter and on the 31st day of December, 1926, pursuant to said application, plaintiff made, issued, executed and delivered to defendant its certain policy of insurance, a copy of which is attached to the Answer and Counterclaim on file herein and by this reference said policy is made a part hereof.

## III.

That by mutual mistake said policy of insurance so issued to defendant was not the policy of insurance applied for by defendant, nor the policy intended to be issued by plaintiff.

## IV.

That a copy of the policy of insurance applied for by defendant is attached to the Complaint on file in this action, marked Exhibit "C", and by this reference is made a part hereof.

## V.

That plaintiff does not keep any copies of policies



issued by it to its assureds and did not keep any copies of the [18] policy issued by it to defendant, and nothing in plaintiff's records would disclose the mistake in furnishing the wrong policy form to defendant; that plaintiff's first knowledge of said mistake was in the month of March, 1946, when said policy of insurance became the subject of discussion between plaintiff and the assignee of said policy of insurance, The Crocker First National Bank of San Francisco.

As and for a further separate answer and defense to said Counterclaim, plaintiff alleges:

### I.

Special reference is hereby made to the allegations of Paragraphs I, II, IV and V of the first further and separate answer and defense to said Counterclaim and by this reference each and all of the allegations thereof are incorporated and made a part of this further and separate defense with like force and effect as if fully set forth herein in full.

### II.

That by mistake of plaintiff, which defendant at the time knew or suspected, said policy of insurance so issued did not truly express the intention of the parties thereto in this that said policy was not the policy of insurance applied for by defendant nor the policy intended to be issued by plaintiff.

Wherefore, plaintiff prays judgment as prayed for in its Complaint herein.

JOSEPH T. O'CONNOR,

HAROLD H. COHN,

Attorneys for Plaintiff. [19]

State of California,

City and County of San Francisco—ss.

Joseph T. O'Connor, being first duly sworn, deposes and says:

That he is one of the attorneys for the plaintiff in the foregoing action; that he has read the foregoing Answer to Counterclaim and knows the contents thereof; that the same is true of his own knowledge, except as to the matters therein stated on information or belief and as to those matters he believes it to be true; that this verification is made by affiant and not by said plaintiff for the reason that said plaintiff and all officers authorized to swear oaths on its behalf are absent from the City and County of San Francisco in which City and County the attorneys for said plaintiff have their offices.

JOSEPH T. O'CONNOR

Subscribed and sworn to before me this 27th day of November, 1946.

[Seal]

LOUIS WIENER,

Notary Public in and for the City and County of San Francisco, State of California.

(Admission of Service)

[Endorsed]: Filed Nov. 29, 1946. [20]

United States District Court for the Northern  
District of California, Southern Division

No. 26322-S

THE TRAVELERS INSURANCE COMPANY,  
Plaintiff,

vs.

GEORGE H. RICHARDSON,  
Defendant.

OPINION AND ORDER

Defendant on December 13, 1926, was insured under two life insurance policies issued by the plaintiff. On that date he signed an application for an "insurance annuity, age 65, on the uniform premium plan" in the principal amount of \$10,000. The premium called for by such a policy at the then age of the defendant was \$287.50 per year. This type of policy was based upon an insurance unit of \$1,000 and entitled insured at the maturity age to receive a cash payment of \$390 for each \$1,000 of insurance and a paid up contract payable at death for \$1,000. The insured was also entitled to receive for each \$1,000 of insurance at maturity age and in lieu of all other privileges, a cash payment of \$1,083. Plaintiff alleges, and the court finds, that it erroneously selected the wrong printed form of policy and instead of the "insurance annuity, age 65, on the uniform premium plan" there was issued to the defendant by the plaintiff a policy known as "pension policy, age 65." The pension policy was based on an insur-

ance [21] unit of \$500 and contained a special privilege entitling the insured at the age of 65 to receive \$739 per year for each \$500 of insurance and a paid up contract payable at death for \$500; in lieu of all of the other privileges under this form of policy the insured was entitled to receive at the maturity age for each \$500 of insurance, a cash payment of \$1083. Yearly premium for this policy at the defendant's then age was \$467.50.

Premiums called for in the policy as issued have been paid yearly by defendant. It appears that the plaintiff keeps no copies of policies issued and the testimony indicates that the company's records did not disclose the error. The records which are kept merely indicate the assured's name, the type of policy and the premium which he is to pay thereon. The mistake was not discovered until March, 1946, when a bank, to which defendant had applied for a loan submitting the policy as collateral, inquired of the plaintiff as to the cash value of the policy. It does appear, however, that on four other occasions the policy had been sent to the home office of the plaintiff for accommodation of the defendant on account of loans made to the defendant. By way of explanation as to why plaintiff did not discover the error on the other times that the policy was in its possession, the testimony indicates that when the policies were received they were referred to a department of the plaintiff which checks merely upon the cash or loan value and registers the assignment for the purpose of the loan. It is shown that that department has no connection with the



issuing department or the policy writing department and that the table of loan values was correct for the insurance annuity policy and that there was no occasion, in making loans on the policy, to refer to the special provisions of the policy where the error was located. The evidence further discloses that at the time [22] of applying for the policy the defendant was an insurance agent, listed as such under the laws of the State of California, and was working under a contract for the plaintiff soliciting insurance. The defendant claims that he was with the plaintiff for less than a year as such agent and that his work during that period was almost exclusively in writing accident insurance. The evidence is in conflict as to whether, during such period of employment, he received training in life insurance in a school of instruction which it appears was maintained by the plaintiff for its agents, or that he had in his possession a manual issued by plaintiff to its agents which describes the different forms of policies, rates, privileges, loan values, etc. It is apparent that the premiums upon the policies which the defendant had prior to December 13, 1926, were burdensome and it would seem that defendant was anxious to surrender those policies for their cash value and take out a new policy calling for a lower premium.

The plaintiff in this action seeks to reform the policy to embrace only the provisions above outlined to an insurance annuity, age 65, on the uniform premium plan.

Preliminary consideration must be given to the

position taken by the defendant relative to the incontestable condition contained in the policy. That provision reads: "This contract shall be incontestable after one year from date of issue, except for non-payment of premiums." The first reported case that dealt with the problem as to whether an action to reform is within such a clause as represented in this case is *Columbian National L Ins. Co. v. Black* 35 F. 2d 571. There, as here, a reformation was sought. The court pertinently observed that it would hardly be suggested that an assured who brings an action to reform a policy was [23] contesting the policy within the meaning of a clause of the same import. The court added that the clause was not one sided and that the right to have the contract express the actual agreement is as available to the assured as to the assurer. The court further stated that although an actual contest may not be found under the cloak of reformation still an action to correct a purely clerical error in the policy issued so as to speak truthfully the agreement is not embraced within the incontestable clause. To the same import see the later cases of *Young v. Met. Life Ins. Co.* 28 Ohio N.P.N.S. 179 and *New York Life Ins. Co. v. Street* 265 S.W. 397. Since the instant action is one in reformation seeking to have the policy express truthfully the agreement between the assured and assurer, an action to reform is not intended or understood to be included within the prohibited contests and is not effected by the above mentioned provision.

An insurance policy comes within the general rule under which a contract is subject to reformation in a proper case if through fraud or mistake it does not express the true agreement. *Genuser v. Ocean Accident & Guarantee Corp.* 57 Cal. 29 App. 2d 979; *Pacific Indemnity Co. v. Industrial Accident Comm.* 29 Cal. App. 2d 414. Although an unilateral mistake is not ground for the relief, (*Metropolitan Life Ins. Co. v. Asofsky*, 38 F. Supp. 464; *Atlantic Life Ins. Co. v. Pharr*, 59 F. 2d 1024) a mistake by one party to the knowledge of the other is equivalent to a mutual mistake. *Mates v. Penn. Mut. Life Ins. Co.*, 55 N.E. 2d 770. *Williston on Contracts*, Vol. 3, Sec. 1497. The knowledge of the mistake on the part of the party against whom reformation is sought must be such as to justify an inference of fraud or bad faith.

I think that the evidence required a finding of mutual mistake. Thirty yearly premiums paid by defendant (the first ten payments being covered by the cash or surrender value of the [24] original two policies) total \$8625. During the twenty years from the writing of the policy in question he was protected by \$10,000 in insurance. If his position is sustained he is now entitled to what he seeks to recover by his counterclaim, the sum of \$21,660. The amount which he would now be entitled to had the policy been issued to him which was applied for is the sum of \$10,830. If he prevails he receives just twice the amount which he would be entitled to under the policy which was ordered and which plaintiff intended to deliver. It is incredible that

defendant did not familiarize himself with the special privileges. He was not a novice in the business world. He admits that he read the policy, apparently shortly after he received it. He had reasons for acquiring the policy. One reason was to afford his family protection. Another was to have an endowment should he reach the age of 65. I am satisfied that he read these provisions and, if he did read them, he must have realized that a mistake had been made. He was an agent of plaintiff, authorized to write just such policies. He must have known that, during the time he would be paying the premiums, a reserve was being set up to meet, when invested, the prospective liability under the policy and that the reserve was prudently invested at low returns. He knew that out of the income of the company is paid its operating expenses. As an insurance agent I am persuaded that he did receive instruction in life insurance writing and that he had readily at his elbow complete information as to the different kinds of policies being written by the company. He was aware that his company could not issue generally the policy which was issued and remain in business. No other conclusion comports with the facts.

But defendant says that he believed, from the statements made to him by the company's agents and officials, that the new [25] policy would pay him substantially the same benefits as the superceded policies conferred. As plaintiff points out, it is impossible for defendant to surrender \$25,000 in policies calling for yearly premiums in excess



of \$500, one of which policies, a \$15,000 policy, matured at age 80, and receive a \$10,000 policy calling for \$287.50 premiums and granting the same rights on his sixty-fifth birthday as provided in the ones surrendered. Besides having had experience in the business world, defendant, his protests to the contrary notwithstanding, had been writing accident insurance for several months and knew something about the insurance business in general and underwriting in particular. I do not believe that such representations were made to him or that he could have understood from anything stated to him that he would receive such benefits. He knew that he applied for a different kind of policy than the one delivered; he must have known the benefits appurtenant to such a policy both at the time he signed the application and at the time he received the policy. The discrepancies between the two are great. The policy revealed to him a patent error.

The conclusion reached is that defendant did notice the error but kept it to himself. The following language in *Columbian Nat. Life Ins. Co. v. Black*, *supra*, may be quoted pertinently:

“While courts are properly reluctant to alter the terms of a written engagement, even in equity, and do not do so unless the proof is clear and convincing, we are of the opinion that uncontradicted and indisputable facts in this case require the interposition of equity. It is true the defendant on the stand and in his letters denies any mistake on his part. But

his actions speak louder than his words. He applied for an ordinary life policy; without any quibble, and in response to his application, he received a policy that manifestly was in error. He only paid for an ordinary life policy. When he received the policy he either did or did not notice the [26] error. If he did notice it, the mistake was mutual. If he did notice it and said nothing, he was guilty of such inequitable conduct as to amount to fraud. A man presents a check for \$100 to a bank teller. He gets two \$100 bills. No matter how loudly he asserts the lack of mistake on his part, the fact still remains that he was either mistaken or was trying to benefit by the teller's mistake. Without resorting to any oral evidence, the papers in this case on their face bear conclusive proof of a mistake that can be and should be corrected in equity."

The argument that the insured would be prejudiced if relief is granted is not appealing. A party to a contract is not prejudiced under any legal acceptance when required to perform his contract. Equity, looking beyond the writing and to the real agreement, sees rather the prejudice to the insurer if the contract were allowed to stand as written.

Finally, laches is raised as a defense. Section 338 of the California Code of Civil Procedure has no bearing. The limitation period there prescribed, by the express wording of the statute, does not begin until discovery of the mistake. Mere lapse of time may not constitute laches which will bar re-

formation, "particularly where the party seeking reformation has been ignorant of the defect which he seeks to have corrected." 44 C.J. S 1116. To constitute laches there must, in addition to lapse of time, appear a prejudice to the adverse party by the enforcement of the asserted right. In *Prudential Insurance Company v. Deane*, 27 Atl. 2d 365, the insurer discovered the mistake twenty years after the policy had been issued. In deciding against the plea of laches the court said, "No prejudice to respondents from the delay of twenty years, nor 'change of situation during neglectful repose' have been demonstrated. Complainant is willing that the insured should have all which [27] he bargained and paid. In consequence, the defense of laches must fall." Defendant states that he is prejudiced because he is now uninsurable, inferring that had the error been discovered years ago when he may have been insurable he could have obtained the protection and benefits through other insurance which he would be deprived of as a result of this action. But this claim is based on the faulty premise that during these years he has hoped and expected to receive twice as much as he applied for and paid for under this policy. "The prejudice results not from the delay but from his ill begotten hope." *Columbian National Life Ins. Co. v. Black*, *supra*.

Judgment will be for the plaintiff as prayed for in its complaint. Defendant will have judgment upon his counterclaim for the sum of \$10,830, or, in lieu thereof for such other benefits as he may

elect to take as provided in the policy as reformed. Findings will be prepared and served by counsel for plaintiff in accordance with the local rule.

Dated: February 6, 1948.

DAL M. LEMMON,

United States District Judge.

[Endorsed]: Filed Feb. 6, 1948. [28]

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[Title of District Court and Cause.]

### FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above entitled cause having heretofore come on regularly for trial before the above entitled Court, and the Honorable Dal M. Lemmon, Judge thereof sitting without a jury, upon the complaint of plaintiff, the answer and counterclaim of defendant to said complaint and the answer of plaintiff to defendant's counterclaim and plaintiff having been present in Court by Joseph T. O'Connor and Harold H. Cohn, its attorneys, and defendant having been personally present in Court and represented by Alvin Gerlack, his attorney, and testimony and evidence having been taken and introduced on the part of plaintiff and defendant, and said cause having been argued by the counsel for the respective parties and submitted to the Court for its decision, and the Court being fully advised now makes the following findings of fact and conclusions of law: [29]



## FINDINGS OF FACT

## I.

That it is true that plaintiff is a corporation duly organized and existing under and by virtue of the laws of Connecticut, and duly authorized to transact the business of life insurance in the State of California; that it is true that plaintiff is a citizen of the State of Connecticut and defendant is a citizen of the State of California; that it is true that the matter in controversy exceeds, exclusive of interest and costs, the sum of \$3000.00.

## II.

That it is true that on the 13th day of December, 1926, defendant applied to plaintiff that there be issued to defendant, an insurance annuity in the amount of \$10,000.00 on the uniform premium plan; that the copy of said application attached to plaintiff's complaint marked Exhibit "A" and made a part of said complaint is a true and correct copy of the application executed by defendant on said 13th day of December, 1926; that the original of said application is in evidence in this action.

## III.

That it is not true that on the 3rd day of January, 1927, plaintiff issued any policy of insurance to said defendant; it is true that on the 31st day of December, 1926, pursuant to said application, plaintiff made, issued, executed and delivered to defendant its certain policy of insurance, a true copy of which except for the erroneous date, to wit,

January 3rd, 1927 instead of December 31st, 1926, is attached to plaintiff's complaint and made a part of said complaint.

#### IV.

That it is true that by mutual mistake, the policy of insurance so issued to defendant by plaintiff was not the policy of insurance applied for by defendant, nor the policy intended to be issued by plaintiff. [30]

#### V.

That it is true that a copy of the policy of insurance applied for by defendant is attached to plaintiff's complaint marked Exhibit "C" and made a part of said complaint.

#### VI.

That it is true that plaintiff does not keep any copies of insurance policies issued by plaintiff to its assureds and it is true that plaintiff did not keep any copy or copies of the policy of insurance issued by it to defendant, and it is true that nothing in plaintiff's records would disclose the mistake in furnishing the wrong policy form to defendant; that it is true that plaintiff's first knowledge of said mistake was in the month of March, 1946, when said policy of insurance became the subject of discussion between plaintiff and the assignee of said policy of insurance, the Crocker First National Bank of San Francisco.

## VII.

That each and all of the allegations of Paragraph I of the second alleged cause of action in plaintiff's complaint are and each of them is true, except that the date of the issuance, execution and delivery of said policy of insurance marked Exhibit "B" and made a part of said complaint, is the 31st day of December, 1926 and not the 3rd day of January, 1927.

## VIII.

That it is true that by mistake of plaintiff, which defendant at the time knew or suspected, said policy of insurance so issued did not truly express the intention of the parties thereto in this, that said policy was not the policy of insurance applied for by defendant, nor the policy intended to be issued by plaintiff.

## IX.

That it is true that the allegations of Paragraph II of the first alleged cause of action in plaintiff's complaint are and each of them is true and correct in all particulars; that it is true that on September 27, 1916 plaintiff made, issued, executed [31] and delivered its policy of life insurance numbered 373735 in the amount of \$15,000.00, which policy provided for annual premiums in the amount of \$309.75; that it is true that on December 13, 1918 plaintiff made, issued, executed and delivered to defendant its life insurance policy numbered 482573 in the amount of \$10,000.00; that it is not true that on or about December 13, 1926 plaintiff prevailed

upon defendant to convert said or any life insurance policies, but it is true that on or about December 13, 1926 defendant applied to plaintiff under the application, a true copy of which is attached to plaintiff's complaint and marked Exhibit "A", that he be permitted in lieu of policies numbered 373735 and 482573 that there be issued to him a new contract of insurance also to be numbered 373735 in accordance with the terms of said application; that it is true that thereafter said plaintiff issued a policy to said defendant, a photostatic copy of which said policy dated December 31, 1926 and effective December 27, 1916, is attached to defendant's answer and counterclaim marked Exhibit 1 and made a part of said answer and counterclaim.

#### X.

That the allegations of Paragraph III of plaintiff's first alleged cause of action are and each of them is true except that the date upon which said policy was made, issued, executed and delivered to defendant is December 31, 1926.

#### XI.

That the allegations of Paragraph IV of the first alleged cause of action in plaintiff's complaint are and each of them is true.

#### XII.

That the allegations of Paragraph V of the first alleged cause of action in plaintiff's complaint are and each of them is true. [32]



XIII.

That the allegations of Paragraph VI of the first alleged cause of action in plaintiff's complaint are and each of them is true; and it is not true that the plaintiff, The Travelers Insurance Company, knew, as early as the year 1927 or at any other time or at all prior to the month of March, 1946, that said policy was issued as set forth in defendant's Exhibit 1 attached to said defendant's answer and counterclaim.

XIV.

That each and all of the allegations of Paragraph I of plaintiff's second alleged cause of action are and each of them is true, save and except that the date upon which said policy of insurance was made, issued, executed and delivered is the 31st day of December, 1926.

XV.

That each and all of the allegations of Paragraph II of said second alleged cause of action in plaintiff's complaint are and each of them is true.

XVI.

That it is not true that plaintiff insurer is guilty of laches; that it is true that at the time defendant converted his said policies numbered 373735 and 482573, he then had a loan on policy numbered 373735 with plaintiff; that it is true that in the month of July, 1928 defendant delivered policy numbered 373735 to plaintiff for the purpose of negotiating a further loan thereon and it is true that plaintiff had said policy in its possession until

the month of August, 1928 but it is true that said plaintiff did not discover any error in said policy while said policy was in its hands for the purpose of negotiating any loan or loans thereon; that it is true that in 1931, defendant negotiated a further loan on said policy numbered 373735 and in the month of September, 1931 delivered said policy to said plaintiff, and that said plaintiff had said policy in its possession and did not return it to defendant [33] until October, 1931; but it is true that said plaintiff did not discover any error in said policy while said policy was in its hands for the purpose of negotiating any loan or loans thereon; that it is true that in 1933 defendant negotiated a loan on said policy numbered 373735 and had said policy in its possession from the month of October to the month of November, 1933 for the purpose of negotiating said loan; but it is true that said plaintiff did not discover any error in said policy while said policy was in its hands for the purpose of negotiating any loan or loans thereon; and it is true that during the year 1936 said defendant negotiated a loan on said policy numbered 373735 and that said plaintiff had said policy in its possession during the month of June, 1936 for the purpose of negotiating said loan; but it is true that said plaintiff did not discover any error in said policy while said policy was in its hands for the purpose of negotiating any loan or loans thereon; that it is not true that by reason of said or any loans, plaintiff well and truly or otherwise, or at all, knew as early as the years 1926, 1928, 1931, 1933, 1936 or at any other time, or at

all, until the month of March, 1946 that said policy numbered 373735 included the "special privileges" provisions in the form set forth in defendant's Exhibit 1 attached to said defendant's answer and counterclaim, but on the contrary said defendant did not know that said "special privileges" provisions was in any other form than the special privileges set forth in Exhibit "C" attached to plaintiff's complaint; that it is true that the premiums on said policy numbered 373735 for \$15,000.00 dated September 27, 1916 were \$309.75 per annum; and it is true that the premiums on policy numbered 373735 dated December 31, 1926 for \$10,000.00 were \$287.50 per annum; that it is not true that the rate charged by plaintiff for said 1926 policy was principally or otherwise on account of any special privileges contained in said policy whatsoever, or at all, but said rate charged was the [34] rate fixed by the uniform premium plan as set forth in plaintiff's "Life Manual" dated January 1, 1916 and for which rate defendant applied; that said plaintiff did not know or suspect and could not by the exercise of reasonable care and/or diligence and/or prudence have known of the exact provisions of said policy; that it is true that plaintiff remained silent for a period of twenty years but said plaintiff had no knowledge of said provisions of said policy until the month of March, 1946; that it is true that defendant performed all of the terms and conditions of said contract including the payment of all premiums called for in said policy before plaintiff brought this suit, but said defend-

ant only performed the terms and conditions on his part to be performed in the policy of insurance applied for by him and did not pay the premiums for any benefits in excess of those called for by the policy applied for by him and did not pay any premiums whatsoever for the benefits mistakenly inserted in the policy delivered to him; that it is not true that as a result of any act or omission of plaintiff whatsoever, defendant has been prejudiced in any manner whatsoever, or at all.

#### XVII.

That it is not true that plaintiff's first and second cause of action or plaintiff's first or second cause of action are, nor is either of them outlawed or barred by the provisions of sections 312 and 338 of the Code of Civil Procedure of the State of California, or either of them or at all; that it is not true that plaintiff's complaint constitutes a stale or outlawed demand.

#### XVIII.

That it is true that by the express terms of said contract of insurance plaintiff is debarred and prohibited from contesting said policy but it is also true that the present suit is not a suit to contest said policy within the meaning of the incontestability clause set forth in defendant's answer and counterclaim. [35]

#### XIX.

That the allegations of Paragraph I of defendant's counterclaim are true.



## XX.

That it is true that on or about the 31st day of December, 1926 plaintiff made and delivered to defendant, its certain policy of insurance numbered 373735 dated December 31, 1926 and effective from September 27, 1916 and insuring the life of defendant, and it is true that the form of said policy delivered by plaintiff to defendant provided that after payment by defendant of thirty annual premiums and defendant's attaining the age of 65 years, said policy provided in words and figures, as follows:

“Special Privileges

“Options Available at Age 65.—The Insured may select in lieu of all other benefits hereunder one of the following options to become available upon the surrender of this contract at its anniversary when the Insured shall have reached the age of 65, the amount of these options being stated for each \$500 of insurance:

1. Receive a cash payment of \$1,083.00
2. Receive a cash payment of \$739.00 and a paid-up contract payable at death for \$500.00
3. Receive a Paid-up contract payable at death for \$1,574.00
4. Receive an annual income of \$112.83 payable during the natural life of the Insured.”

But in this connection, the Court finds that it is also true that said special privileges hereinabove

set forth were inserted in said policy by mutual mistake and by mistake of plaintiff which defendant at the time of execution and delivery knew or suspected and said defendant knew that said policy of insurance so issued did not truly express the intention of the parties thereto in this, that said policy was not the policy of insurance applied for by defendant, nor the policy of insurance intended to be issued by plaintiff. [36]

### XXI.

That it is true that a photostatic copy of said policy is attached to defendant's answer and counterclaim.

### XXII.

That it is true that the express terms of said policy call for the payment to said defendant of the sum of \$21,660.00 but said terms were inserted in said policy by mutual mistake of the parties and by mistake of plaintiff which said defendant at the time knew or suspected, and said policy so issued did not truly express the intention of the parties thereto in this, that said policy provision was not the provision applied for by defendant nor the provision intended to be issued by plaintiff; that the sole agreement of the parties was that plaintiff agreed to pay to defendant the sum of \$10,830.00 and not the sum of \$21,660.00.

### XXIII.

That the allegations of Paragraph VI of said counterclaim are and each of them is true.

## XXIV.

That it is true that defendant attained the age of 65 years on August 21, 1946 and that said policy matured on September 27, 1946.

## XXV.

That it is true that defendant has performed all of the terms and obligations of said contract on his part to be performed under the policy issued to him, but it is not true that he has performed the terms and conditions omitted by mistake from said policy and he has only performed the terms and conditions in the policy of insurance applied for by him; and it is true that plaintiff has failed and refused to pay defendant the sum of \$21,660.00 or any sum exceeding \$10,830.00. [37]

## XXVI.

That it is true that the premiums specified as due on the policy of insurance issued to defendant were not proper premiums for said policy in this, that said premiums were the proper premiums for a policy of insurance carrying with it the right to receive at age 65 for each \$1000.00 of insurance, a cash payment of \$395.00 and a paid-up contract at death for \$1000.00, but not the right to receive at age 65 a cash payment of \$739.00 for each \$500.00 of insurance and a paid-up contract at death for \$500.00.

## XXVII.

That it is true that while defendant has performed the terms and conditions indicated by mis-

take in the policy issued to him, it is also true that he has not performed the terms and conditions omitted by mistake from said policy and it is true that said defendant has only performed the terms and conditions in the policy of insurance applied for by him.

### XXVIII.

It is true that on the 13th day of December, 1926, defendant applied to plaintiff that there be issued to defendant an insurance annuity in the amount of \$10,000.00 on the uniform premium plan and it is true that a copy of said application is attached to plaintiff's complaint on file in this action marked Exhibit "A" and made a part of said complaint.

### XXIX.

It is true that on the 31st day of December, 1926 pursuant to said application, plaintiff made, issued, executed and delivered to defendant its certain policy of insurance, a true copy of which is attached to the answer and counterclaim on file in this action and marked Exhibit 1.

### XXX.

It is true that by mutual mistake, said policy of insurance so issued to defendant was not the policy of insurance applied for by defendant, nor the policy of insurance intended to be issued [38] by plaintiff.

### XXXI.

It is true that a true copy of the policy of insurance applied for by defendant is attached to the



complaint on file in this action and marked Exhibit "C."

XXXII.

It is true that plaintiff does not keep any copies of policies issued by it to its assureds and did not keep any copy or copies of the policy issued by it to defendant, and it is true that nothing in plaintiff's records could or did disclose the mistake in furnishing the wrong policy form to defendant; it is true that plaintiff's first knowledge of said mistake was in the month of March, 1946.

XXXIII.

That the allegations of Paragraph I of plaintiff's second separate answer and defense to said counterclaim are true.

XXXIV.

That it is true that by mistake of plaintiff, which defendant at the time knew or suspected, said policy of insurance so issued did not truly express the intention of the parties thereto in this, that said policy was not the policy of insurance applied for by defendant, nor the policy intended to be issued by plaintiff.

CONCLUSIONS OF LAW

I.

That said policy of insurance numbered 373735 as issued contains special privileges erroneously inserted in said policy by mutual mistake of the parties and by mistake of plaintiff which defend-

ant at the time knew and suspected, in this, that said policy as issued provided as follows: [39]

“Special Privileges

“Options Available at Age 65. The Insured may select in lieu of all other benefits hereunder one of the following options to become available upon the surrender of this contract at its anniversary when the Insured shall have reached the age of 65, the amount of these options being stated for each \$500 of insurance:

1. Receive a cash payment of \$1,083.00
2. Receive a cash payment of \$739.00 and a paid-up contract payable at death for \$500.00
3. Receive a paid-up contract payable at death for \$1,574.00
4. Receive an annual income of \$112.83 payable during the natural life of the Insured.”

instead of providing:

“Special Privileges

“Options Available at Age 65. The Insured may select in lieu of all other benefits hereunder one of the following options to become available upon the surrender of this contract at its anniversary when the Insured shall have reached the age of 65, the amount of these options being stated for each \$1,000 of insurance:

1. Receive a cash payment of \$1,083.00

2. Receive a cash payment of \$395.00 and a paid-up contract payable at death for \$1,000.00
3. Receive a paid-up contract payable at death for \$1,574.00
4. Receive an annual income of \$112.83 payable during the natural life of the Insured."

II.

That plaintiff is entitled to a judgment reforming said policy of insurance so as to express the true intention and agreement of the parties on both plaintiff's first and second causes of action set forth in plaintiff's complaint, together with a judgment for its costs of suit herein expended.

III.

That plaintiff's action for reformation of said policy of insurance is not barred by any statute of the State of California or provision of said policy of insurance.

IV.

That defendant is entitled to a judgment upon his counterclaim for the sum of \$10,830.00 and no more, or in lieu thereof for such other benefits as defendant may elect to take as [40] provided in the policy as reformed.

Let a judgment be entered accordingly.

Dated Feb. 26, 1948.

DAL M. LEMMON,

Judge of the U. S. District  
Court.

[Endorsed]: Filed Feb. 26, 1948.

In the District Court of the United States, for the  
Northern District of California, Southern  
Division

No. 26322-S

THE TRAVELERS INSURANCE COMPANY,  
Plaintiff,

vs.

GEORGE H. RICHARDSON,

Defendant.

### JUDGMENT

The above entitled cause having heretofore come on regularly for trial before the above entitled Court and the Honorable Dal M. Lemmon, Judge thereof, sitting without a jury, upon the complaint of plaintiff, the Answer and Counterclaim of defendant to said Complaint, and the Answer of plaintiff to said defendant's Counterclaim and plaintiff having been present in Court by Joseph T. O'Connor and Harold H. Cohn, its attorneys, and defendant having been personally present in Court and represented by Alvin Gerlack, his attorney, and testimony and evidence having been taken and introduced on the part of plaintiff and defendant and said cause having been argued by counsel for the respective parties, and submitted to the Court for its decision and the Court being fully advised and having heretofore made and rendered its decision in writing, setting forth its Findings of Fact and Conclusions of Law in said cause, which decision, Findings of Fact and Conclusions [42] of



Law have been filed herein, and ordered that judgment be entered in accordance therewith;

Wherefore, by reason of the law and the findings aforesaid:

It is hereby ordered, adjudged and decreed and this Court does hereby order, adjudge and decree as follows, to wit:

That said policy of life insurance issued by plaintiff on the life of George H. Richardson, defendant, which said policy is numbered 373735 as issued contains special privileges erroneously inserted in said policy by mutual mistake of the parties and by mistake of plaintiff which defendant at the time knew and suspected as follows:

#### “Special Privileges

“Options Available at Age 65.—The Insured may select in lieu of all other benefits hereunder one of the following options to become available upon the surrender of this contract at its anniversary when the Insured shall have reached the age of 65, the amount of these options being stated for each \$500. of insurance:

1. Receive a cash payment of \$1,083.00
2. Receive a cash payment of \$739.00 and a paid-up contract payable at death for \$500.00
3. Receive a Paid-up contract payable at death for \$1,574.00
4. Receive an annual income of \$112.83 payable during the natural life of the Insured.”

And it is further ordered, adjudged and decreed and this Court does hereby order, adjudge and decree that said policy of insurance should have provided as issued for special privileges as follows:

“Special Privileges

“Options Available at Age 65.—The Insured may select in lieu of all other benefits hereunder one of the following options to become available upon the surrender of the contract at its anniversary when the Insured shall have reached the age of 65, the amount of these options being stated for each \$1,000 of insurance:

1. Receive a cash payment of \$1,083.00
2. Receive a cash payment of \$395.00 and a paid-up contract payable at death for \$1,000.00
3. Receive a Paid-up contract payable at death for \$1,574.00
4. Receive an annual income of \$112.83 payable during the natural life of the Insured.” [43]

It is further ordered, adjudged and decreed that said policy of insurance be reformed so as to express the true intention and agreement of the parties on both plaintiff’s first and second causes of action by inserting in lieu of the special privileges inserted in said policy as written, the following special privileges:

“Special Privileges

“Options Available at Age 65.—The Insured may select in lieu of all other benefits here-

under one of the following options to become available upon the surrender of the contract at its anniversary when the Insured shall have reached the age of 65, the amount of these options being stated for each \$1,000 of insurance:

1. Receive a cash payment of \$1,083.00
2. Receive a cash payment of \$395.00 and a paid-up contract payable at death for \$1,000.00
3. Receive a Paid-up contract payable at death for \$1,574.00
4. Receive an annual income of \$112.83 payable during the natural life of the Insured."

It is further ordered, adjudged and decreed that neither of plaintiff's causes of action for reformation of said policy of insurance is barred by any statute of the State of California or provision of said policy of insurance; and

It is further ordered, adjudged and decreed that defendant above named do have and recover judgment from plaintiff for the sum of Ten Thousand Eight Hundred Thirty (\$10,830.00) Dollars together with interest thereon as provided by law from September 27, 1946 and no more, or in lieu thereof, for such other benefits as defendant may elect to take as provided in said policy as reformed; and

It is further ordered, adjudged and decreed that plaintiff above named do have and recover from defendant above named, its costs of suit expended in the sum of \$ .

Dated: February 26th, 1948.

DAL M. LEMMON,

United States District Court  
Judge.

The foregoing Judgment is hereby approved as to form as provided in Rule 5 (d).

ALVIN GERLACK,

Attorney for defendant.

[Endorsed]: Filed Feb. 26, 1948. [44]

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[Title of District Court and Cause.]

#### NOTICE OF APPEAL

Notice is hereby given that George H. Richardson, Defendant above named, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit from the final judgment entered in this action on February 27, 1948.

/s/ ALVIN GERLACK,

Attorney for Defendant and  
Appellant.

[Endorsed] Filed Mar. 26, 1948. [45]



[Title of District Court and Cause.]

STATEMENT OF POINTS ON WHICH APPELLANT INTENDS TO RELY ON APPEAL

Now comes the above named Defendant and Appellant and pursuant to Subdivision (d) of Rule 75 of the Federal Rules of Civil Procedure files this, his designation of the points on which he intends to rely on his appeal herein to the United States Circuit Court of Appeals for the Ninth Circuit:

1—The said District Court erred in finding that the Plaintiff (Appellee) was not guilty of laches in instituting this present action in 1946 when it had the clear opportunity, in 1926 when it issued the policy, and again in 1928, 1931, 1933 and 1936 to discover the claimed error in the issuance of the policy, but nevertheless waited some 19 years after issuance of the policy before bringing this action.

2—The District Court erred in finding and concluding that the California Statute of Limitations, Code of Civil Procedure Sections 312 and 338 did not apply to the instant action.

3—That said District Court erred in finding that the “incontestable clause” of the policy did not apply to the present suit in the instant case.

4—The said District Court erred in finding that the Plaintiff (Appellee) only discovered for the first time the claimed error in the policy in 1946. In view of the District Court’s finding XVI that the Plaintiff (Appellee) had the policy in his possession four times, namely July and August 1928,

September and October 1931, October and November 1933 and June 1936, the said District Court's findings are inconsistent and contradictory in the following respects to wit:

Finding XVI finds the Plaintiff had the insurance policy in question in its possession in its San Francisco and also in its home office in Hartford, Connecticut in connection with policy loans four different times, namely 1928, 1931, 1933 and 1936, whereas finding XVI also finds that the Plaintiff (Appellee) discovered the claimed mistake of the issuance of the policy for the first time in March 1946 and the said District Court erred in rendering judgment for the Plaintiff (Appellee) based upon such inconsistent and contradictory findings.

5—The said District Court erred in ordering judgment for the Plaintiff (Appellee) in view of the Plaintiff's (Appellee) admitted examination of the policy in question in July and August 1928, September and October 1931, October and November 1933, and June 1936, and the Trial Court's finding XVI to that effect, and what Appellant claims is a clear and unmistakable case of laches on the part of the Plaintiff and (Appellee). [47]

6—The District Court erred in finding that the Defendant (Appellant) was not prejudiced by the Plaintiff (Appellee) waiting 19 years and collecting all of the 20 annual premiums due under the policy and further waiting until the Defendant (Appellant) was almost 65 years of age and obviously uninsurable before bringing the present action.

7—The District Court erred in finding that the policy of insurance was issued through mutual mistake of parties hereto and/or that the policy was issued by mistake of Appellee (Plaintiff) which Appellant (Defendant) at the time knew or suspected and also in finding that the policy as issued was not the policy applied for by the Appellant (Defendant), and in finding that the special privileges inserted in the policy by the Appellee (Plaintiff) was by mutual mistake of the parties and/or by mistake of the Appellee (Plaintiff) which appellant (Defendant) at the time knew or suspected.

/s/ ALVIN GERLACK,

Attorney for Defendant and  
Appellant.

[Admission of Service.]

[Endorsed: Filed Apr. 8, 1948. [48]]

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[Title of District Court and Cause.]

DESIGNATION OF CONTENTS OF  
RECORD ON APPEAL

Comes now the above named Defendant and Appellant and pursuant to the provisions of Rule 75 of the Federal Rules of Civil Procedure, files this, his designation of the portions of the Record and Proceedings to be contained in the Record on his Appeal herein to the United States Circuit Court of Appeals for the Ninth Circuit:

1. Caption
2. Names and addresses of counsel
3. The complaint of Plaintiff
4. The answer and counterclaim of the Defendant
5. The answer of the Plaintiff to Defendant's counterclaim
6. Opinion of the Trial Court
7. The findings of fact and conclusions of law made by the trial court [49]
8. Judgment of the Trial Court
9. Notice of Appeal
10. The designation of Contents of Record on Appeal
11. Statement of points on which Appellant intends to rely on appeal
12. Certified Reporter's transcript of all proceedings at trial of this action.

Dated this 8th day of April, 1948.

ALVIN GERLACK,  
Attorney for Defendant.

It is so stipulated

JOSEPH T. O'CONNOR,  
HAROLD H. COHN,  
Attorneys for Plaintiff.

[Endorsed]: Filed Apr. 8, 1948. [50]



In the District Court of the United States  
Northern District of California

**CERTIFICATE OF CLERK TO TRANSCRIPT  
OF RECORD ON APPEAL**

I, C. W. Calbreath, Clerk of the District Court of the United States, for the Northern District of California, do hereby certify that the foregoing pages, numbered from 1 to 52, inclusive, contain a full, true, and correct transcript of the records and proceedings in the cause of *The Travelers Insurance Co. vs. George H. Richardson*, No. 26322 S, as the same now remain on file and of record in my office.

I further certify that the cost of preparing and certifying the foregoing transcript of record on appeal is the sum of \$5.20, and that the said amount has been paid to me by the Attorney for the appellant herein.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court at San Francisco, California, this 30th day of April, A. D. 1948.

[Seal]

C. W. CALBREATH,

Clerk,

/s/ E. H. NORMAN,

Deputy Clerk.

In the District Court of the United States for  
the Northern District of California, Southern  
Division

No. 26322-S

THE TRAVELERS INSURANCE COMPANY,  
Plaintiff,

vs.

GEORGE H. RICHARDSON,  
Defendant.

Before: Hon. Dal M. Lemmon,  
Judge.

REPORTER'S TRANSCRIPT

Thursday, October 16, 1947

Appearances:

Joseph T. O'Connor, Esq., and Harold H. Cohn,  
Esq., for Plaintiff.

Alvin Gerlack, Esq., for Defendant.

The Clerk: Travelers Insurance Company vs.  
Richardson.

Mr. Cohn: Ready.

Mr. Gerlack: Ready.

The Court: Proceed.

(Thereupon counsel made opening state-  
ments.)

Mr. Cohn: Will you stipulate that this is the  
application?

Mr. Gerlack: Yes. That is his signature. [1\*]

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\* Page numbering appearing at top of page of original Reporter's  
Transcript.

The Court: Offer it in evidence.

Mr. Cohn: The plaintiff will offer it in evidence under stipulation.

The Court: It may be admitted and marked.

(The application is marked Plaintiff's Exhibit 1.)

Mr. Gerlack: It is stipulated that is the application on which the policy was issued.

Mr. Cohn: Yes.

Mr. Gerlack: It is also stipulated that is not in the handwriting of Mr. Richardson except the signature.

Mr. Cohn: Yes, if that is the fact.

Mr. Gerlack: That is a fact is it not, the signature is the only thing in your handwriting?

Mr. Richardson: Yes.

Mr. Gerlack: We will stipulate that a policy was in fact issued.

Mr. Cohn: You will stipulate that this was the policy that was issued.

Mr. Gerlack: Yes.

(The policy was marked Defendant's Exhibit A.)

The Court: Is it stipulated that the amounts called for in the policy were paid?

Mr. Cohn: Yes.

Mr. Gerlack: I call your attention to the fact that there are no payments called for in the application.

Mr. Cohn: The application does not say anything about the premium. The application only

states the form of policy [2] that is applied for.

The Court: Are there any other stipulations that counsel may suggest?

Mr. Gerlack: Will you stipulate that the Home office had the policy in its possession four different times?

Mr. Cohn: Yes, we admit that, but we will show that when a policy goes to the company for a loan it goes to an entirely different division; it goes to the policy loan division which has nothing to do with the policy writing division.

Mr. Gerlack: We think that is immaterial.

The Court: Is there any other stipulations you want to make?

Mr. Cohn: I don't know whether counsel is willing to do it or not but I will ask him: will you stipulate that the premium called for by this policy was not the premium called for by the pension form of policy, or do you want me to prove it?

Mr. Gerlack: I cannot stipulate to that; I have no facts on which to base it.

The Court: Call your first witness.

### HAROLD WATERMAN

called for the plaintiff; sworn.

The Clerk: Will you state your name to the Court?      A. Harold A. Waterman.

Q. (By Mr. Cohn): Mr. Waterman, where do you reside?

A. Waterford, Connecticut, a town adjoining Hartford. [3]



(Testimony of Harold A. Waterman.)

Q. What is your business?

A. I am Assistant Secretary of the Travelers Insurance Company.

Q. In Hartford, Connecticut? A. Yes.

Q. You have you been with it how long?

A. I have been with the Travelers Insurance Company for thirty-one years.

Q. How long have you been Assistant Secretary? A. Three years.

Q. Are you connected with any particular branch or department of the company? A. Yes.

Q. What department or branch are you connected with?

A. Life underwriting department.

Q. Is that the department of the company that handles life insurance? A. Yes.

Q. Now, Mr. Waterman, are you familiar with the practice of the company with respect to keeping policies of insurance? A. Yes.

Q. What is the practice of the company in this regard?

A. Our practice in that regard is to keep a master form of all policies that the Travelers Insurance Company has issued since its inception. [4]

Q. Do you keep copies of every individual policy of life insurance that you issue to a policyholder?

A. No, we do not.

Q. What is the practice of the company? How do you know what a policy really is? Will you explain that to the court?

A. I might answer that in this way, when the

(Testimony of Harold A. Waterman.)

application, examination, and other papers incidental to the file arrive in the Home Office they are all assembled together; they pass through the various departments, up to the point of underwriting; that is the point where we decide as to the acceptability of the policy; if the application is approved the file then moves on to what we call our issuing or policy writing division. At that point there is a detail of the various features in connection with the issue of the contract, such as the policy form to be issued, the cash value which was to be put in that particular contract, and any other features which might be incident to the issue of such a policy.

Q. Now when the policy is issued to an insured what record do you make of that, if any?

A. We have in that file what we call a stub with the name of the individual, the branch office, and all underwriting data is kept in that file, that is up to the point of underwriting procedure; following that underwriting another stub is placed over the top of the original stub, and that [5] stub shows the policy form of contract which presumably has been issued and the premium for the coverage in its entirety. From that we establish records which are sent to our various departments necessary for the future handling of that particular issue.

Q. Do I understand then Mr. Waterman, that this is what you retain, the stub?

A. We retain the whole file, the complete file in every case of a policy that has been issued right

(Testimony of Harold A. Waterman.)

on through from the application on; everything incident to the case.

Q. What you mean is this, you do not keep a copy of the policy, do you?      A. No, we do not.

Q. Incidentally do you photograph copies of the policy?      A. No, we do not.

Q. How do you know then what kind of a policy has been issued?

A. The only record we have is in connection with the stubs and it is assumed from this data record that each individual who has handled the file has done his job properly and correctly and that is the actual contract.

Q. But you do not have the contract.

A. We do not have the contract.

Q. Will you explain to the court the various steps that an application goes through from the time that the application is approved until the policy itself is issued?

A. The mechanics of the issuance of a policy of life insurance, [6] after the risk has been approved, is that, the file is picked up and moved out to our issuing division; at that point the policy form, the cash value to be used and any other features incident to the issue of the contract are assembled and placed in the file; the case then goes to what we call our stub clerk who sets up the coverage desired and then goes on to the examiner to check the work of the stubber, to make sure that no error has occurred. From that point it goes on to what we call our issuing department.

(Testimony of Harold A. Waterman.)

Q. Would your memorandum, in referring to it, disclose any mistake or error in the policy as issued as far as the terms of it are concerned?

A. No, it would not.

Q. Mr. Waterman, are you familiar with the types of policy issued by The Travelers Insurance Company in 1926 and 1927? A. Yes.

Q. And are you familiar with the policy form that you call your Insurance Annuity?

A. Yes.

Q. Are you also familiar with your policy form known as Pension Insurance, age 65?

A. Yes.

Q. How do you determine the premium which is to be charged for these respective policies? [7]

A. By the amount of exposure on the risk, and on the insurance annuity you have \$1,000 and on your pension contract you have \$500, and you have to take into consideration the annuity portion of the contract, and the premium is based on that.

Q. After determining the premium to be charged for any particular form of insurance do you put that data in any book?

A. Do you have reference to individual cases?

Q. No, in general I mean?

A. Yes, we have a Manual which we issue which shows the proper premium charges for all contracts which we issue.

Q. What is the name of the manual?

A. It is known as Life Manual.



(Testimony of Harold A. Waterman.)

Q. In there are set forth the various premiums charged for the various forms of policy?

A. That is correct.

Q. Now, are you familiar with the premium charge for an annuity policy, and which is known as Insurance Annuity at 65, as issued by the company in 1926 and 1927?      A. Yes.

Mr. Gerlack: Is that the one you showed me?

Mr. Cohn: I was going to lay a foundation for it.

Q. Is that the Manual that covers this policy for 1926?

A. Yes, I think that is the Manual that was in force when that contract was issued.

Mr. Cohn: I offer the rate manual in evidence.

The Court: Admitted.

(The life manual is marked Plaintiff's Exhibit 2.)

Q. (By Mr. Gerlack): That was in force in 1926 when the policy was issued?      A. Yes.

Q. It applies to this policy?

A. It applies to that policy of insurance.

Q. This calls for a premium of \$287.50 plus \$48.10 for permanent total disability?

A. That is correct.

Q. That is taken out of that manual?

A. Yes.

Q. (By Mr. Cohn): What is the \$287.50 premium for?

A. The \$287.50 is for the insurance annuity policy.

(Testimony of Harold A. Waterman.)

Q. What is the unit? A. \$1,000.

Q. Does that manual also disclose the premium for the pension form of policy? A. It does.

Q. And what is the unit for the pension form?

A. \$500.

Q. What is the premium on that?

A. \$23.38.

Q. For what? A. Per \$500. [9]

Q. And ten times would be what?

A. \$233.80.

Q. That would be for each \$500. A. Yes.

Q. And for \$1,000 you double it, is that correct?

A. Yes.

Q. Which would make it \$467.60?

A. Yes, I believe so.

Q. At any rate it would be twice that?

A. It would be twice that, whatever it is; it would be \$467.60.

Q. When you issue a contract in life insurance what do you do? Do you keep a master form of contract?

A. Yes, we have a master form of contract of every policy ever issued by The Travelers Insurance Company.

Mr. Cohn: You may cross-examine.

#### Cross-Examination

By Mr. Gerlack:

Q. Mr. Waterman, will you please state what steps the policy goes through that is issued? Let me ask you this: you are familiar with that application; you have seen it before? A. Yes.

(Testimony of Harold A. Waterman.)

Q. That application goes through the local office?

A. Yes.

Q. And then it goes to Hartford, Connecticut, the Home Office? A. Yes.

Q. Then what happens to it? [10]

A. When the application, the examination and all other papers incident to the policy are received they are all assembled together and go through the various channels up to the actual underwriting procedure.

Q. How many people in the local office would have occasion to see it?

A. Probably just one.

Q. How many people in the Home Office would see it before it was finally issued? How many people would probably see that policy?

A. With reference to that particular point, three, the underwriter, the stubber and the man who examines the file.

Q. Do you have somebody that looks it over before it goes out, a final investigator?

A. No.

Q. Now some of the insurance companies, I understand, do micro-film each policy that is issued.

Mr. Cohn: I am going to make an objection.

Mr. Gerlack: This is cross-examination.

A. I don't know of any company that makes microfilms of policies issued.

Q. Your company does not? A. We do not.

Q. Every government check that is issued is micro-filmed before [11] it is released, is it not?

(Testimony of Harold A. Waterman.)

A. I don't know.

Q. That is a regular and customary procedure, is it not?      A. I don't know.

Q. Now, as I understand life insurance premiums are supposed to be based on the American Tables of Mortality, is that correct?

A. Not entirely.

Q. In general that is true?

A. That is a part of the method of fixing the premium.

Q. Now then you load that up with your office overhead, your agent's commission and your office expenses?      A. Yes.

Mr. Cohn: I cannot see the materiality of this testimony.

Mr. Gerlack: That is one of their contentions, that this man got something he did not pay for. That is to show that the rates they charge for policies vary. That is correct, isn't it?

A. They vary.

Q. What commission does your company pay on a policy such as this, for the original premium?

A. I am not familiar with our commission scale so I could not answer that question.

Q. As a matter of fact it is fifty or sixty per cent of the premium, is it not?

A. It is not, in some cases.

Q. In this type of policy do you know what is paid or was paid [12] in 1926 when this policy was written?      A. I do not recall.



(Testimony of Harold A. Waterman.)

Q. Whatever the commission might be would be reflected in the premium?

A. Yes, that is part of the cost of the contract.

Q. There are no two companies that have the same commission,—I mean for a comparable policy; it varies with the overhead, office salaries and other expenses of the company and also the profit which is paid to the stockholders of the company?

A. That is true in part, but another company may charge the same premium for the same type of contract.

Q. That is very unusual, is it not?

A. Not at all.

Q. For instance, your company pays the president \$250,000 a year salary, does it not?

A. I don't know.

Mr. Gerlack: That is all.

### Redirect Examination

By Mr. Cohn:

Q. Mr. Waterman, I show you Defendant's Exhibit A and I will ask you to examine it and I will call your specific attention to the Special Privileges section of the policy. I also call your attention to the premium. A. Yes.

Q. Will you take a look at the cash surrender and loan value table? [13] A. Yes.

Q. Have you examined those? A. I have.

Q. Now, will you refer to your Life Manual and tell me first of all what is the premium called for on that policy? Is it the premium called for on an annuity policy or pension policy?

(Testimony of Harold A. Waterman.)

A. It is the premium called for on our Insurance Annuity,—65 contract.

Q. And the table of loan value of the policy, does that refer to the annuity or pension form?

A. It refers to the annuity.

Q. Referring to your Life Manual is the pension form different from the annuity form as to the loan value?      A. Yes, it is.

Q. Referring to the Special Privileges section of the policy,—I am referring now to Option No. 2, and also to the insurance annuity of the policy, is that the annuity or the pension form?

A. That is the pension form.

Mr. Cohn: That is all.

#### Recross-Examination

By Mr. Gerlack:

Q. Mr. Waterman, I neglected to ask you what department of The Travelers are you in?

A. Assistant Secretary of the life department.

Q. What does that mean? [14]

A. Just that—anything to do with the issuing and handling of life insurance contracts.

Q. You mean writing the policies?

A. Underwriting and the writing of the contracts.

Q. Were you in that position in 1926 when this policy was issued?

A. I was then serving in the capacity of chief underwriter of the company.

Q. So this policy came through your department?      A. Definitely.

(Testimony of Harold A. Waterman.)

Mr. Gerlack: I think that is all.

Further Redirect Examination

By Mr. Cohn:

Q. I would like to ask one question if I may. I refer you to Plaintiff's Exhibit 1, Mr. Waterman; what is that an application for?

A. That is a request for changing an existing contract which is done in every case where an individual wants to change existing coverage carried in a company.

Q. What change is requested, what type of contract?

A. He asked us that the contract be changed to \$10,000 insurance Annuity age 65.

Q. Insurance Annuity age 65? A. Yes.

Mr. Cohn: That is all.

Mr. Gerlack: That is all.

The Court: We will take a short recess. [14A]  
(After recess.)

Mr. Cohn: Your Honor, by stipulation of counsel, at this time for the purpose of establishing that the Crocker National Bank had the policy, I am offering in evidence an assignment by Mr. Richardson and his wife of the policy to the bank; that assignment has since been released.

Mr. Gerlack: What date is that?

Mr. Cohn: April 21, 1937.

Mr. Gerlack: There is no objection to putting that in.

The Court: It may be admitted and marked.

(The assignment is marked Plaintiff's Exhibit 3.)

Mr. Cohn: There is no objection to putting in the release which is dated July 30, 1946.

Mr. Gerlack: I offer it as Defendant's Exhibit.

The Court: It may be admitted and marked.

(The release is marked Defendant's Exhibit B.)

Mr. Gerlack: I might say the object of putting in the last exhibit is to show that from 1937 to 1946, July 30, the policy was not in Mr. Richardson's hands but in the hands of the Crocker National Bank.

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JAMES A. WEIGHTMAN

called for the Plaintiff; sworn.

The Clerk: Will you state your name to the court?

A. James A. Weightman. [15]

Q. (By Mr. Cohn): Your name is James A. Weightman? A. Yes.

Q. You are employed by The Travelers Insurance Company, are you? A. Yes, I am.

Q. In what capacity?

A. Assistant Cashier in the San Francisco Branch Office.

Q. Is that the division of the company that handles loans? A. Yes.

Q. I will ask you whether or not in the year 1946 you had some communication or talk with the



(Testimony of James A. Weightman.)

Crocker National Bank regarding the insurance policy which is the subject matter of this lawsuit?

A. Yes, I did.

Q. Can you tell us about when that conversation or talk took place? A. About March, 1946.

Q. Can you tell us who it was with?

A. I believe it was Mr. Creeley.

Q. Of the Crocker National Bank?

A. Yes.

Q. What was the subject matter of that conversation?

Mr. Gerlack: Just a minute. May I ask was the defendant Mr. Richardson there, present at that conversation? A. No. [16]

The Court: The objection is overruled. What was the subject matter of that conversation?

A. We received an inquiry from the bank as to the value under the Special Option in the contract and we in turn told him what the special options were according to the record of the policy in our Home Office.

Q. Did the Crocker National Bank subsequently show you the contract that they had?

A. Yes, I am pretty sure that they did.

Q. Would your records indicate that, after refreshing your recollection on that point?

A. Yes, they did permit us to look at the contract.

Q. And is that the first time that you had seen the special privilege portion of the contract that Richardson had? A. Yes, it was.

(Testimony of James A. Weightman.)

Q. When you saw that what did you do?

A. I wrote to the Home Office of our company and advised them that we had been permitted to inspect the contract and that in my opinion the options were incorrect for an insurance annuity 65 form of contract.

Q. Then did you receive certain instructions from your Home Office?

A. Yes, I did. They said that my interpretation of the options were correct and asked me to write to the person concerned, [17] Mr. Richardson, and request the return of the contract for correcting for those errors.

Q. When was that?

A. Could I look for the date?

Q. Yes.

A. The Home Office wrote to me giving me this advice on March 29, 1946.

Q. What was the date of your communication to the Home Office?      A. March 22, 1946.

Q. When was your communication with the Crocker National Bank?

A. That was not in writing. Those were telephone conversations and one conversation at our office with a representative of the Crocker National Bank just prior to March 22; it might have been that day or one or two days prior to that, but approximately that time.

Q. Then did you follow the Home Office instructions?

(Testimony of James A. Weightman.)

A. Yes, I wrote to Mr. Richardson according to the instructions on April 4, 1946.

Mr. Cohn: Do you have that letter, the original?

Mr. Gerlack: What date?

Mr. Cohn: A letter dated April 4, 1946, to Mr. Richardson.

Mr. Gerlack: I will stipulate to save time that they entered into a controversy after the company wrote to Mr. Richardson asking him to return the policy, and he refused and we had some discussion back and forth on which there was no agreement. [18]

Mr. Cohn: I will accept that stipulation. I want to ask one further question in that regard.

Q. Pursuant to one of your letters—you wrote a number, did you? A. More than one.

Q. Did Mr. Richardson come into the office of The Travelers Insurance Company? Do your records show that? By "the office" I mean the office at 315 Montgomery Street, San Francisco?

Mr. Gerlack: I have the original letter.

A. About May 16, 1946, I saw Mr. Richardson in our office. Does that answer your question?

Q. (By Mr. Cohn): Yes. At that time did he say anything to you about surrendering the policy for correction?

A. He said that it was his plan to let the matter ride until the maturity of the policy.

Q. Now then, do you handle loans for The Travelers Insurance Company? A. Yes, I do.

Q. On policies? A. Yes, I do.

(Testimony of James A. Weightman.)

Q. Will you state whether or not the loan division of the company is the same or different from the underwriting division?

A. They are different departments.

Q. And in the Home Office of the company they are different?

A. They are separate departments.

Q. Do you personally handle the making of loans on policies? [19]      A. Yes, I do.

Q. In making loans on policies do you have any occasion to refer to the Special Privileges section of the policy?      A. No.

Mr. Gerlack: We will object to that as immaterial, irrelevant and incompetent. They had the opportunity to do that.

The Court: The objection is overruled.

A. We have no occasion to look at the section of the policy which refers to Special Privileges at maturity in order to make loans because they have no bearing on the loan value.

Q. (By Mr. Cohn): What does have bearing on the loan value?

A. There is a table in the policy headed "Cash and Loan Values" and that is what they refer to, the number of the policy, the insured's name, to be sure that we have the correct contract, and then we refer to the table of the loan value in the policy which is entirely separate from the Special Privileges Section; and we refer to that and calculate the loan value.



(Testimony of James A. Weightman.)

Q. In other words you do not read the whole policy in order to make a loan on it?

A. No. The policyholders would get very slow service on loans if we had to stop and do that.

Mr. Cohn: That is all.

Cross-Examination

By Mr. Gerlack:

Q. Mr. Weightman, did you handle the loan in 1929? [20] A. No, I did not.

Q. Did you handle the loan in 1931?

A. No, I did not.

Q. Didn't it go through your office?

A. It went through our office but I did not handle it.

Q. The option form was in the policy all the time and if you had looked at it you could have seen it, couldn't you?

Mr. Cohn: I will object to that.

The Court: Overruled.

Q. (By Mr. Gerlack): The option is a part of the policy; it is not a rider, is it?

A. No, it is a part of the policy.

Q. It is the usual form that is used; it is on the back of the front page, isn't it? A. Yes.

Q. It is not attached as a rider? A. No.

Q. Mr. Weightman, did you handle the correspondence with Mr. Richardson regarding the policy?

A. I handled some of it and our Home Office handled some of it.

(Testimony of James A. Weightman.)

Q. Did you receive the original of that letter from Mr. Richardson with this attached to it?

Mr. Cohn: May I see them.

Mr. Gerlach: Pardon me. [21]

Q. I assume you received the original of that?

Mr. Cohn: I will stipulate that he received the original.

A. That is right.

Mr. Gerlach: May I offer this in evidence?

Mr. Cohn: Yes.

Mr. Gerlach: It is dated April 10, 1946. 111 Sutter Street. Rm. 930, San Francisco, California.

“The Travelers Insurance Company,  
315 Montgomery Street,  
San Francisco 4, California.

Attention J. A. Weightman, Assistant Cashier.

Gentlemen:

I acknowledge receipt of your letter of April 4, 1946, regarding my policy No. 373735.

I wish to advise that the policy contract which I hold reads ‘The amount of these options being stated for each \$500 of insurance,’ not ‘for each \$1,000 of insurance,’ as you state in your letter.

Very truly yours,

GEORGE H. RICHARDSON.”

Mr. Cohn: What is the date of that letter?

Mr. Gerlach: April 10, 1946.

Q. You say the first time, as far as you know,

(Testimony of James A. Weightman.)

that somebody discovered this, the plaintiff discovered this, was in March, 1946?

A. Yes. [22]

Q. That was after the company had collected premiums on the original policy and collected the premiums on the present policy?

A. Yes, I believe that is right.

Q. There was nothing further for Mr. Richardson to do to perform his part of the insurance contract except to reach sixty-five years of age?

A. That is my understanding.

Q. He paid all the money and the only thing that was to be performed on Mr. Richardson's part was to live to be sixty-five years of age, which was, I think, August 21, 1946?

A. I don't know about the date.

Mr. Gerlack: I think that is all.

Mr. Cohn: That is all. [23]

Mr. Cohn: I would like to call Mr. Richardson for cross-examination.

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GEORGE H. RICHARDSON

the defendant; sworn.

Cross-Examination

By Mr. Cohn:

Q. Mr. Richardson, you are the defendant in this action, are you? A. Yes.

Q. The same George H. Richardson, who is

(Testimony of George H. Richardson.)

named as the insured in the policy which is the subject matter of this litigation; that is correct, is it not?      A. Yes.

Q. Mr. Richardson, directing your attention to the year 1926, you were an agent of The Travelers Insurance Company, were you not?      A. Yes.

Q. You were an agent authorized to sell life insurance among other forms of insurance, were you not?      A. I must have been.

Q. Well, you were, were you not?

A. I had the privilege of delivering contracts of life insurance, I know, so I must have had the privilege of placing them.

Q. You had a signed contract with the company, didn't you?

A. Yes, I had a signed contract.

Q. That was to sell life insurance, was it not?

A. Show me the contract with my signature, and I will say whether I was or not. This is twenty years ago.

Q. Will you take a look at this contract?

A. Yes.

Q. That is the contract that you signed on or about the date it bears, is that right?      A. Yes.

Q. To wit July 12, 1926, is that correct?

A. Yes.

Q. That contract authorized you to sell life insurance, did it not?      A. Yes.

Q. You resigned from the company December 31, 1927?

A. That is right, December 31, 1927.



(Testimony of George H. Richardson.)

Q. December 31, 1927, that is what it says.

A. Yes.

Mr. Cohn: They are clipped together, your Honor. I will offer them as one exhibit.

Mr. Gerlack: No objection.

The Court: They may be admitted and marked.

(The contract and resignation are marked Plaintiff's Exhibit 4.)

Q. (By Mr. Cohn): You were also licensed by the State of California to sell life insurance in July, 1926, were you not? A. I believe so. [25]

Q. And at or about the time that you applied for this policy of life insurance which is the subject matter of this lawsuit, or, rather, prior to that time, you had, among others, two policies with The Travelers Insurance Company, did you not?

A. I believe so.

Q. And those two policies were encumbered by loans, were they not? A. Apparently.

Q. Well, you know that, don't you, Mr. Richardson?

A. I don't. There were two contracts involved.

Q. I am referring to the two policies, Mr. Richardson, that you surrendered to the company at the time that you got the contract which is the subject matter of this lawsuit?

A. There was a loan on this 37 contract, but whether there was on the other your records would show.

Q. Now, you had been with the company how long at the time that you signed the application,

(Testimony of George H. Richardson.)

Plaintiff's Exhibit 1 in this case, for the contract which is the subject matter of this lawsuit?

A. Your records would show.

Q. Don't you know, Mr. Richardson, how long you had been with the company?

A. How long I had been with the Travelers?

Q. Yes, aside from what the records may show?

A. No. [26]

Q. Haven't you any idea, Mr. Richardson?

A. It is twenty-one years ago and some months.

Q. Now, you were with the Travelers in the capacity of a soliciting agent, isn't that correct?

A. Correct.

Q. And you had recently made your connection with the Travelers?      A. Yes.

Q. And business was not so good with you at that time?      A. Where? With the Travelers?

Q. Yes?

A. As far as I was concerned the only instruction I received from the Travelers was to solicit accident insurance and the extent of the business would show I was doing pretty good for a new man.

Mr. Cohn: I move to strike that out as not responsive.

Mr. Gerlack: He made a statement in there that he was doing pretty good for a new man.

Q. (By Mr. Cohn): You were having trouble making the premium payments on the two contracts that you ultimately surrendered for this one, were you not?      A. I don't believe so.

Q. Do you know a Mr. Whitaker?

(Testimony of George H. Richardson.)

A. Yes.

Q. He was a field assistant with the Travelers at the time we are referring to, was he not?

A. He was in what I would call an official capacity; whether he was field assistant or assistant manager I would be unable to state.

Q. He assisted you in making the transfer, didn't he?

A. That is something I don't know.

Q. You would not say it was not so?

A. I would not, no.

Q. You never discussed the pension form of insurance with whoever assisted you at any time, did you? A. I don't know. [27]

Q. Wasn't this your thought at the time that you applied for the transfer of insurance, to get as much insurance protection as you could, eliminate the loans, at the smallest possible premium?

A. No. I was suggested this coverage. I had \$25,000 worth of protection for my family in the two policies that became the foundation of this one policy which I surrendered for \$10,000 protection.

Q. Now, Mr. Richardson, isn't this a fact, that you had discussed with whoever assisted you in making this change that you were going to surrender these policies that you had? A. No.

Q. You did not do that? A. No.

Q. You did not discuss with them the fact that you were going to surrender the two policies you had and take out a new one—you did not discuss that with anyone? A. I would say no.

(Testimony of George H. Richardson.)

Q. Isn't it a fact, Mr. Richardson, that you discussed with whoever assisted you that you wanted to get all the cash you could out of the two policies that you had and take out a new policy of insurance?      A. No.

Q. That isn't true?      A. No.

Q. Now, while you were an agent of the Travelers Insurance Company and before you became active in this field you [28] received training in reading the manual Plaintiff's Exhibit 2?

A. No.

Q. From no one?

A. To the best of my knowledge, no.

Q. Without confining you to this particular manual did you ever see any insurance manual of the Travelers Insurance Company like that?

A. No.

Q. Did you ever receive any training whatsoever in the reading of this insurance company manual?

A. No.

Q. No one took you over the ground and showed you how to read it?      A. No, they didn't.

Q. Yet you were employed as a life insurance agent under your contract?

A. Agent for the Travelers Insurance Company.

Q. You left the Travelers Insurance Company at the end of 1927, is that right?

A. Your records would indicate that.

Q. That is the date of your resignation there is it not?      A. December 31, 1927.



(Testimony of George H. Richardson.)

Q. Did you receive any training in life insurance between July 12, 1926, and December 31, 1927?

A. No. [29]

Q. None whatsoever?

A. Not to the best of my recollection.

Q. Mr. Richardson, subsequent to the time that you left the Travelers Insurance Company, namely, on October 26, or about that date, 1928, you took out another policy with Travelers Insurance Company, did you not?           A. Yes.

Q. You were your own agent, that is, I mean you did not do that through any agent at all?

A. I would not recall that at all. Was that a business policy? Who are the beneficiaries?

Q. This is a policy in the amount of \$5,000 payable on your life.

A. That was a personal policy of mine.

Q. You did not have any agent for that? You took that out yourself, isn't that right?

A. I would not recall that.

Mr. Gerlack: That is permissible under the laws of California.

Mr. Cohn: I am not offering it for that purpose.

Q. In 1928 you took out a second \$5000 policy with the company? Is that right?

A. I would not recall.

Q. On December 15, 1931, you took out a \$2000 policy with the company, didn't you?

A. No. [30]

Q. That is not so?           A. No.

(Testimony of George H. Richardson.)

Q. On the same date, December 15, 1931, you didn't take out a \$2,000 policy with the company?

A. No.

Q. That isn't so?                      A. It is not so.

Q. Without referring to specific dates, but within a very short time after you left the Travelers Insurance Company you took out a number of policies with the Travelers Insurance Company yourself, did you not, on your life?

A. I don't know what you mean by a number, but I have always been a great believer in life insurance.

Q. When I say "a number" I mean two or three or four insurance policies? Didn't you take out a number with the Travelers Insurance Company?

A. Your records would indicate.

Q. Don't you know, Mr. Richardson? You had the policies, you know that, don't you?

A. No.

Q. You don't know that?                      A. No.

Q. You recognize that you could have not have taken out insurance that you did not know anything about?                      A. I know I paid premiums. [31]

The Court: You took out a policy in 1926. What is your recollection as to policies you took out later with the Travelers Insurance Company?

A. I know there were two on my life and I think there was a business policy taken out.

Q. (By Mr. Cohn): Now on all of those policies you acted as your own agent, isn't that so?

A. I don't know.

(Testimony of George H. Richardson.)

Q. You mean to tell me that you took out insurance policies and you don't know who the agent was that wrote them?

A. Your records would show that.

The Court: Counsel is asking for your recollection.

A. I answered him, I don't know.

Q. (By Mr. Cohn): Let me ask you this question: isn't it a fact that you have taken out a number of policies at or about the time you severed your connection with the Travelers Insurance Company in which you did act as your agent?

A. I don't know.

Q. Do you mean to tell me, Mr. Richardson, that you don't know that, and that is your answer to that question?

A. Yes.

Mr. Cohn: I think that is all at this time.

Mr. Gerlack: That is all at this time. We will put our case on. [32]

## GERALD WHITAKER

called for the Plaintiff; sworn.

The Clerk: Will you state your name to the court.

A. Gerald Whitaker.

Q. (By Mr. Cohn): Where do you live, Mr. Whitaker?

A. I live at 800 Contra Costa Avenue in Berkeley.

(Testimony of Gerald Whitaker.)

Q. What is your business?

A. I am manager of the Travelers Insurance Company's Oakland branch office.

Q. Were you also connected with the Travelers Insurance Company in November, 1926?

A. Yes.

Q. Where were you located at that time?

A. I was in the San Francisco branch office as a field assistant in the agency department.

Q. At or just prior thereto did you make the acquaintance of Mr. Richardson, the defendant in this lawsuit?

A. Yes.

Q. What was his business at that time?

A. At that time Mr. Richardson was an agent of the Travelers Insurance Company in the San Francisco branch office.

Q. Were you the person who assisted him in changing over his policy?

A. I was.

Q. Did you know that he was already insured with the Travelers Insurance Company? [33]

A. Yes.

Q. How did you know that?

A. He showed me his Travelers' policies which had been taken out in another branch office.

Q. Do you know what his condition was as far as making payment of premium on these policies? Did he discuss that with you?

A. Yes. He had two policies, one about ten years old and the other about eight; one was for \$15,000 and the other was for \$10,000; and there were loans on both policies, and being somewhat of



(Testimony of Gerald Whitaker.)

a new agent with the Travelers and his income not being much as yet, he wanted to change the policies so that he would have a lesser premium and either lessen the loan or have the loan wiped out entirely.

Q. Did he discuss the possibility that he might give the policies up altogether?

A. He did.

Q. What did he say in that regard, as near as you can recall?

A. He at first planned to take the equity, and by "equity" I mean present cash value left after the existing loan and apply it to a new policy at his then age in 1926, and I suggested that we communicate with our home office to see if we could change the policy and protect his original age so that he would have the amount of insurance that he desired, which was \$10,000 and have the benefit of the rate in force when he was ten years younger. [34]

Q. Now what form of policy did you discuss? Did you discuss annuity, pension or what?

A. We discussed what we call our insurance annuity maturing at the age of sixty-five.

Q. Was that the type of policy that you suggested to him? A. Yes.

Q. How did that come about, do you recall?

A. I don't recall exactly but it probably came out after discussing the many types of contract that we had, and decided on a policy that the premium would be within his means at that time.

(Testimony of Gerald Whitaker.)

Q. You conducted the negotiations with the home office on that?      A. I did.

Q. I will ask you, Mr. Whitaker, did you write to the home office on this matter?      A. I did.

Q. What information did you give them?

A. I advised them of Mr. Richardson's condition; I advised them that he was an agent, that he had \$25,000 life insurance with the Travelers, that he desired a \$10,000 policy on the annuity plan and asked them to prepare figures for us whether or not it was more advantageous to take the rate in 1916 or the 1926 rate.

Q. Did they subsequently communicate with you?

A. They did; they mailed to me the figures showing the premium [35] for the \$10,000 policy, how the loan would be reduced from the amount on the \$25,000 to the amount on the \$10,000.

Q. Are these the figures that you received?

A. Yes.

Q. This is a duplicate, is it not?

A. Yes—that is a carbon copy.

Q. It is a carbon copy of what they sent you?

A. Yes.

Q. You showed that to Mr. Richardson just as it is?

A. Yes. I showed it to him and talked it over with him.

Mr. Cohn: I will offer this in evidence, your Honor.

The Court: It will be received.

(Testimony of Gerald Whitaker.)

(The memorandum is marked Plaintiff's Exhibit 5.)

Q. (By Mr. Cohn): I notice that it says "Annual premium 335.60" on the proposed new contract?

A. Yes.

Q. That is broken down. So that the court will be clear on this the \$48.10 is for what?

A. For a disability provision that provides for waiver of premium and income of \$100 a month.

Q. Then the balance of the premium is on what?

A. On the annuity insurance at the age of 65.

Q. The total is \$335.60?

A. The total is \$335.60.

Q. Did Mr. Richardson agree that was the form of insurance that he wanted with you?

A. He did. [36]

Q. And authorized you to procure it?

A. Yes.

Q. I show you Plaintiff's Exhibit 1; did you prepare that?

A. I did.

Q. And had Mr. Richardson sign it?

A. Yes.

Q. Now, in November, 1926, were you connected with the agency department of the Travelers?

A. Yes.

Q. Did you have anything to do with the training of new agents?

A. I did.

Q. Will you state what training, if any, was given to agents in life insurance?

A. They were trained in what we call manual

(Testimony of Gerald Whitaker.)

drill; that is, so they would be familiar with the rate manual, the premium rate; they were also trained in sales talk or sales ideas.

Q. Were the various forms of contracts issued by the company at that time the subject matter of any training? A. Yes.

Q. Were they explained to the life insurance agents? A. They were.

Mr. Cohn: You may cross-examine.

#### Cross-Examination

By Mr. Gerlack:

Q. How many insurance policies have you had personal contact and experience with in the last twenty-one [37] years since this conversation with Mr. Richardson? A. Many.

Q. Do you recall all the details of each and every one of the different transactions as vividly as you have detailed the conversation with Mr. Richardson? A. No.

Q. As a matter of fact you never personally explained his duties there, did you?

A. I believe that I assisted Mr. Richardson as an agent as I did many other agents in the San Francisco branch office.

Q. Regardless of what the contract says he was employed for the purpose of soliciting accident insurance solely, was it not?

A. No, sir. He was employed to represent us in our life insurance department as well as the accident department.



(Testimony of Gerald Whitaker.)

Q. While it was possible for him to write policies in the life department, and he was privileged under his license from the State of California to write life insurance, his duties ostensibly called on him for writing accident insurance, isn't that correct?

A. Yes, but they are licensed to write for all departments.

Q. Now getting back to the time that this policy was issued, the total premium on the \$15,000 policy was \$309.75, isn't that correct?

A. I would have to look at the letter which shows the amount of premium. [38]

Q. He was paying for \$15,000 of insurance under the policy which was converted \$309.75, is that correct?      A. Yes.

Q. That included \$48.10 for total permanent disability?

A. No. Permanent total disability was already on it; when he made the change it was on the other contract. There were two policies.

Q. Do you know where the original contract is?

Mr. Cohn: I have it here, if you want it.

Q. (By Mr. Gerlack): As to the \$309.75, which was the \$15,000 policy, the rate he was paying on that was \$0.35 a thousand, was it not?

A. \$20.65.

Q. \$20.35 is pretty close. Now the premium on the present policy was \$287.50; the premium on that was \$28.75 per thousand, is that correct?

A. The annual premium would be that.

(Testimony of Gerald Whitaker.)

Q. Therefore, under the present policy the premium rate was more than \$8.00 more per thousand than the premium rate on the \$15,000 policy, which was \$20.65? A. Yes.

Q. Per annum? A. Yes.

Q. When did the transactions you have told us about with a great [39] deal of detail, when you discussed the transfer matter with Mr. Richardson—when did that take place?

A. After reviewing the file so my memory would be refreshed, I would say it was at the time that this change was made.

Q. You have no specific independent recollection of that?

A. No. It is only after a review of our files.

Q. Are you basing that conversation you had on these records or are you relying on independent recollection that you had irrespective of the records?

A. No; I am basing it on our records after reviewing the file.

Q. You presume from what the records show you must have had this conversation?

A. I reviewed the letter that I wrote the home office asking their recommendation on this matter, their reply to me, and subsequent letters, along with the contract.

Q. If it was not for the records you would not remember? A. No.

Mr. Gerlack: I think that is all.

Mr. Cohn: That is all. Plaintiff rests.

The Court: We will take a recess until two o'clock. [40]

Afternoon Session

GEORGE H. RICHARDSON

recalled for defendant.

By Mr. Gerlack:

Q. Mr. Richardson, you have previously been sworn?      A. Yes.

Q. Just to clear up your connection with the Travelers Insurance Company, when did you come to San Francisco?      A. 1922.

Q. What was your occupation from then on to 1926?

A. I was manager of Naumberg & Company's office in San Francisco—they are a New York Company.

Q. What was their business?

A. Commercial paper and notes.

Q. Pretty much the same business as you are in now?

A. It was a business in which commercial paper and notes were sold.

Q. Any way you were in——

A. Financial business.

Q. How did you come to go with the Travelers Insurance Company?

A. Naumberg & Company closed their Pacific Coast office, and having been in California for four years I did not want to go back East.

Q. Then an opportunity presented itself with the Travelers?      A. Yes. [41]

Q. And you went with them?      A. Yes.

(Testimony of George H. Richardson.)

Q. At the time you signed that contract with the Travelers is that the usual type of contract with agents?

A. I took it for granted that it was.

Q. The same type? A. Yes.

Q. That gave you a right to sell and get a commission on all policies issued by the Travelers, did it? A. Yes.

Q. What kind of business did Travelers have you solicit and do?

Mr. Cohn: I object to that since there is no proper foundation laid for it.

The Court: That is too general.

Q. (By Mr. Gerlack): You went with the Travelers in what department? What type of insurance did you solicit for them?

A. They put me at selling accident insurance.

Q. Did you actually sell life insurance?

A. I took what they told me to do; I was working for them.

Q. Originally did you ask to sell life insurance for them? A. Yes.

Q. When they asked you to sell accident insurance did they give you any reason why they did not permit you to sell life insurance?

A. I was strictly on a commission basis and it was evidently [42] their thought that accident commissions would help a man to live. I was strictly on commission.

Q. How much commission did you get on the accident policies? A. Twenty-five per cent.



(Testimony of George H. Richardson.)

Q. Did you have any drawing account?

A. No.

Q. You sold policies and got twenty-five per cent commission and that is all? A. Yes.

Q. Did they give you any rate manual or anything to carry with you?

A. I am sure I had an accident manual.

Q. How many types of accident policies did you sell? A. Two particularly.

Q. Was it necessary to look in the manual to find a man's age or anything of that character in connection with these policies? A. No, sir.

Q. Was there a flat premium or did the premiums vary on the policies?

A. I would call it a flat premium; that is, they paid \$25 a week disability or \$5,000 in case of accidental death; that was \$25 premium.

Q. Did the amount of the premium depend on the age? A. No. [43]

Q. Just a flat rate policy? A. Yes.

Q. It covered practically all injuries?

A. When a man reaches sixty the premium goes up.

Q. But the ordinary man you solicited you did not have to look up what the premium was?

A. No.

Q. For that reason it was not necessary to have that manual, is that correct? A. Yes.

Q. When you went there did they give you any training or any schooling to learn the accident insurance business?

(Testimony of George H. Richardson.)

A. They had I think what you would call on-the-job training; that is, one of the assistant managers would go out with you.

The Court: Counsel's question was, did they give you any training when you first went to work for them?

A. No.

Q. (By Mr. Gerlack): You did not go to school for a period of time to learn the business?

A. No.

Q. Did they give you any literature or anything like that?      A. Yes.

Q. What were those?

A. Well, just folders describing the two types of accident policies.

Q. It had nothing to do with life insurance?

A. No.

Q. You said you had job training; what did you mean by that?

A. Well, as I said, one of the assistant managers would go out with you and make calls with you.

Q. Was that Mr. Whitaker?

A. No. There were two men, you might say, my bosses.

Q. Who were they?

A. Mr. Clendenan and Mr. Hensley.

Q. Do you know where Mr. Clendenan is now?

A. No.

Q. Have you seen them from that time to this?

A. I have seen Mr. Hensley from time to time,

(Testimony of George H. Richardson.)

but I have not seen him in a number of years. He is I believe down on the Peninsula and you tried to get in touch with him.

Q. You attempted to get in touch with him?

A. You tried to.

The Court: Answer the question.

Q. (By Mr. Gerlack): You attempted to get in touch with him? A. Yes.

Q. Now did you know of your own knowledge at the time you were with the Travelers Insurance Company what was their practice in regard to training so far as soliciting is concerned?

A. To train them as they trained me.

Q. That did not include any instruction in how to use the life rate manual? [45] A. No.

Q. Now, how did you get along as an agent for the company soliciting this accident insurance after you went to work in July, 1926?

A. Fairly well.

Q. When did you cease your duties actively as an agent?

A. The early part of 1927 you might say I set up my own business along the line of what I had been in previously.

Q. How long had you been in this previous business with Naunberg & Company?

A. I was with them from 1904 practically the entire time to 1926 when they closed their office here.

Q. In 1926? A. Yes, 1926.

Q. The business you are now engaged in is the business you started in the spring of 1927?

(Testimony of George H. Richardson.)

A. Yes.

Q. Therefore you were in a dual capacity during the year 1927, I understand, of being on the rolls of the company as an accident soliciting agent of the company and carrying on your own business?

A. That is correct, except that I was giving practically all my time to my own business.

Q. Do you recall how you came to formally resign on December 31, 1927? [46]

A. Well, I think I felt that I should give all of my attention to my own business, and divorce myself from the insurance business.

Q. Why did you give up the insurance business?

A. Well, I am afraid I was not the type that makes a real success of the insurance business.

Q. Did you feel that you were not suited to be in the insurance business? A. Yes.

Q. You recall the loans that have been testified to here? A. Yes.

Q. Do you recall whether the company had the policies or whether they had been returned to you?

A. I would not be able to state on that. I know they had them but when they came back to me I don't recall.

Q. You do recall that the policies went back to the company?

A. Absolutely; it was the practice for the policies to go back to obtain a loan on the policies.

Q. Now, Mr. Richardson, do you recall the circumstances under which you changed these poli-



(Testimony of George H. Richardson.)

cies, the \$25,000 worth of insurance and took this policy of \$10,000 with the special option?

A. My recollection is——

Q. Just tell his Honor how this all happened, how it came about? [47]

A. My recollection is that I discussed it with some of the men down at Travelers and I was told that there was a policy that they felt might fit in as well with my requirements and I would cease paying premiums at the age of 65, and that there were options in that policy by which if I lived to 65 I would receive practically the same benefits as I would receive from the life policies which were replaced by this present policy.

Q. What were these policies, what were the types of them?

A. \$10,000 ordinary life and \$15,000 cash settlement at the age of 80.

Q. That is \$15,000 at the age of 80?

A. Yes. Those two policies that I replaced represented \$25,000.

Q. Do I understand you to say then that the understanding that you came to with the Travelers Insurance Company in the fall of 1926 was that you could get this present policy which would afford you \$10,000 and have the benefits and options that you would with the \$25,000 policies? A. Yes.

Q. Was that the definite understanding with the officers of the Travelers?

Mr. Cohn: Your Honor, I would like to make an objection to that question on the ground there

(Testimony of George H. Richardson.)

is no proper foundation laid for it and it calls for a conclusion.

The Court: It calls for an opinion and conclusion.

Q. (By Mr. Gerlack): What was the position with the Travelers of both Mr. Glendenin and Mr. Hensley? [48]

A. I would say that they were assistant managers.

Q. In what department?

A. Well, they specialized on life insurance so far as my understanding was.

Q. What advice did they give you insofar as changing or dropping the \$25,000 policies and taking the \$10,000?

A. Well, that I would benefit myself by the fact that the premium ceased at the age of 65, when the policy matured, and that so far as I was concerned that after 65, if I lived, that I would receive practically the same amount as I would on the other policies.

Q. In other words that was a definite understanding from your discussion with Mr. Clendenin and Mr. Hensley? A. Yes.

Q. What was done after that, after you had this discussion? You showed them your present policies, did you?

A. I would not be able to recall on that; they had that data on the policies in their file; whether I had the policies or not I don't know.

(Testimony of George H. Richardson.)

Q. At that time the policies were in the company's files?      A. Yes.

Q. Did you come to a definite understanding with them concerning the type of new policy you were to get?

A. Well, I took the policy that had been suggested to me as the equivalent of what it replaced.

Q. (By The Court): What do you mean by the term "equivalent." It took \$25,000 to get \$10,000; that was not equivalent. What do you mean by "equivalent"?

A. Well, that the option was such on that policy, the \$10,000 policy, that if I lived to be 65, that sofar as I was concerned I would receive under the option the same benefits as I could have received under the \$25,000.

Q. (By Mr. Gerlack): That was their representation to you at the time?

A. That was my understanding.

Q. Now what happened after you reached that understanding?

A. Well, I signed an application.

Q. Who worked out the mechanics of that?

A. Mr. Whitaker testified he did and I have no question but that his statement is correct.

Q. Do you recall talking to him personally about it?      A. I don't until outside this morning.

Q. But the understanding you had was with Mr. Clendenin and Mr. Hensley?      A. Yes.

Q. Now, the complaint alleges in paragraph 4 "that by mutual mistake said policy of insurance

(Testimony of George H. Richardson.)

so issued to defendant was not the policy of insurance applied for by defendant, nor the policy intended to be issued by plaintiff." Was there any mistake, so far as you were personally concerned in your [50] understanding of the type of policy you would get?

Mr. Cohn: I object to that question on the ground it calls for a conclusion.

The Court: It calls for a conclusion. Let him give the conversation.

Q. (By Mr. Gerlack): You examined the policy which is the basis of this lawsuit?

A. Yes.

Q. Was it your understanding that that was the type of policy you were to get when you had this conversation with Mr. Clendenin and Mr. Hensley?

A. Yes.

Q. And was it your understanding that that policy you got, and on which you paid twenty premiums—was it your understanding that you would take that type of policy and pay the premiums on, when you had this understanding with Mr. Clendenin and Mr. Hensley?

Mr. Cohn: I object to the understanding the witness says he had with those two gentlemen. How does he know that they were assistant managers.

Q. (By Mr. Gerlack): Do you know their positions?

A. I would not be able to state their titles but I think there is a gentleman here who could testify exactly to what they were.



(Testimony of George H. Richardson.)

Q. At any rate, whatever representations they made to you [51] they made on behalf of the Travelers Insurance Company, is that right?

A. Yes, the representation made to me was that I was making a change advantageous to myself in that I was through paying the premiums at age 65 on that policy——

Q. (By the Court): You received this policy, did you?      A. Yes.

Q. I assume you looked it over at the time you received it, did you not?

A. In a very cursory way.

Q. Was there anything in the cursory examination of that policy that called your attention to the fact that there was any difference between that policy and the others that you had?

A. Absolutely not.

Q. Or the application that you signed?

A. Absolutely not.

Q. (By Mr. Gerlack): I notice that counsel made a great point that this application says "Amount \$10,000 insurance annuity age 65 on the Uniform Premium Plan with No. A Disability Provision." Did you discuss or was that drawn to your attention, or was anything said about that technical term "Insurance annuity age 65" at the time you had the discussion with Mr. Clendenin and Mr. Hensley or with Mr. Whitaker?

A. My recollection would be that at the age of 65 they called to my attention the fact that I could take an income of \$1,000 [52] a year or surrender

(Testimony of George H. Richardson.)

the policy for whatever value the policy gave me which he stated to me was available but I had to reach the age of 65.

Mr. Gerlack: I think that is all.

Cross-Examination

By Mr. Cohn:

Q. Mr. Richardson, when you were questioned by the court you said that you read this policy when you got it?

A. If I so said I wish to apologize for my statement.

Q. How long after you got your policy did you read it? A. I did not read my policy.

Q. If I misunderstood you I want you to correct me: I understood you in reply to the question by the court to say when the policy was delivered to you you looked it over cursorily?

A. I looked it over cursorily, but by reading it I take it you mean as you would read a book.

Q. Let me ask you this, you recall your deposition being taken in this case? A. Yes.

Q. Would you read page 11 line 22?

A. "Mr. Cohn: Q. "—"——

Q. Read it to yourself?

A. I beg your pardon. Yes.

Q. I will ask you if on October 14, 1946, this question was asked you to which you gave this answer: "Can you give us any idea of approximately how long ago it was that you read this policy of insurance for the first time, Mr. Richardson?

A. No sir."

A. Yes.

(Testimony of George H. Richardson.)

Q. And the following question "In other words, it may have been one month ago or it may have been twenty years ago, is that correct? A. I didn't read it twenty years ago."

Q. You gave those answers to those questions at that time, is that correct? A. That is correct.

Q. Now Mr. Richardson, you said that you began in business with this company,—I did not quite catch the name?

A. Naumberg & Company.

Q. That was in 1904, was it? A. 1904.

Q. Part of the business of that company was making loans on policies of insurance, wasn't it?

A. Yes.

Q. That is the same business you are in today?

A. It is part of the business I am in.

Q. Part of your business is negotiating loans on life insurance policies is it not?

A. That is correct.

Q. For clients of yours?

A. That is correct.

Q. And that was the business you were in in 1927, was it not? A. It was not. [54]

Q. What did you mean when you said you were in the same business today as you were with Naumberg & Company?

A. I did not say the same; I said similar.

Q. When did you first start negotiating loans on life insurance policies? A. In 1929.

Q. That was the first time? A. Yes.

(Testimony of George H. Richardson.)

Q. Now in 1929 you were familiar with life insurance business, were you?

A. As a policy holder, yes.

Q. Well, you were a licensed agent, weren't you?

A. Yes, it would appear so.

Q. To sell life insurance? A. Yes.

Q. And you said that is what you wanted to do when you went with the Travelers? A. Yes.

Q. And they would not let you? A. Yes.

Q. Did you have any specific hours of employment? A. No.

Q. You could come and go and work at other things, is that right?

A. As far as hours of employment are concerned my hours of employment have always been to be at the office at starting [55] time in the morning and leave at a certain time at night.

Q. (By The Court): You had no specific hours of employment? A. No.

Q. (By Mr. Cohn): As far as accident insurance was concerned they did not give you leads, but you could go to anybody? A. Yes.

Q. You could submit applications to the company from any one? A. Yes.

Q. So that when you told this court they would not let you write life insurance that was strictly up to you as to what to do?

A. My reply to that would be that my training has been to do what my instructors tell me to do.

Q. They didn't tell you to do anything, did they?

A. Yes.



(Testimony of George H. Richardson.)

Q. Did somebody tell you what to do?

A. Yes.

Q. Who?

A. I was turned over to Mr. Hensley and Mr. Clendenin to be my instructors and I did as my instructors told me.

Q. There was no instruction as to the method that you should use? A. No.

Q. In other words they told you what you could sell and what you could not sell, is that right? [56]

A. They suggested it to me in the instructions.

Q. Didn't they also give you some training as to what these various policies were?

A. Not that I can recall.

Q. Will you read on page 13 line 3?

A. Yes.

Q. I will ask you if when your deposition was taken this question was asked you, to which you gave this answer:

“Q. Now, Mr. Richardson, when you went to work for the Travelers Insurance Company as a contract agent, you were given some training before you were sent out into the field, isn't that correct?

A. Correct.” Didn't you so testify?

A. Is the length of time stated there?

Mr. Gerlack: I think the proper question is to ask the witness if he made the statement and give him an opportunity to explain.

Mr. Cohn: I was going to do it but he did not give me a chance.

(Testimony of George H. Richardson.)

A. My testimony I think fully agrees with my deposition.

Q. Just let me read this into the record.

“Q. Now, Mr. Richardson, when you went to work for the Travelers Insurance Company as a contract agent, you were given some training before you were sent out into the field, isn’t that correct?      A. Correct.

“Q. And who gave you that training, do you know?

“A. Chris Hensley, Norman Clendenin.

“Q. Of what did your training consist, Mr. Richardson?      A. Accident insurance.

“Q. Did they explain anything about policies of life insurance to you?      A. Yes.”

Now did you give that testimony at the time of the taking of your deposition?      A. Correct.

Q. Regardless of whether that training was in the field in the life insurance or accident insurance you were given training before you were sent into the field, isn’t that so?

A. Training occupying a brief six hours.

Q. Maybe we do not understand each other?

A. No, I do not.

Q. You can answer this question yes or no, can’t you? Regardless of what you testified to in your deposition is it not a fact that policies of insurance, whether accident or life or whatever the case might be were shown to you and explained to you?

A. As to accident insurance.

(Testimony of George H. Richardson.)

Q. Did they send you any literature for you to read?      A. I would not recall.

Q. Do I understand your testimony as you sit there, and correct me if I am wrong, that you did not get any training as far as life insurance was concerned,—nobody explained the policy to you?

A. That is correct.

Q. But at the same time you were a licensed agent to sell life insurance?      A. Yes.

Mr. Cohn: That is all.

Mr. Gerlack: That is all. That is our case.

The Court: Is there any rebuttal?

Mr. Cohn: I would like to recall Mr. Whitaker for a question.

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## GERALD WHITAKER

recalled for Plaintiff.

By Mr. Cohn:

Q. Mr. Whitaker, did you receive any commission or any compensation at any time for assisting Mr. Richardson in changing over his policies?

A. No.

## Cross-Examination

By Mr. Gerlack:

Q. What commission does the company pay on life insurance?

A. If the contract is less than \$2500 it is fifty per cent commission; if the contract is \$2500 or more the commission first year is 55 per cent; the

(Testimony of Gearld Whitaker.)

renewal commission may be five per cent for four years or five per cent for nine years or three per cent for nine years, depending on the type of contract.

Q. Mr. Whitaker, did you know Mr. Clendenin?

A. Yes. [59]

Q. And Mr. Hensley? A. Yes.

Q. During the year 1926 what was their connection and title with the company?

A. Mr. Clendenin was assistant manager in charge of the life, accident and annuity department in the San Francisco branch office.

Q. And Mr. Hensley?

A. Mr. Hensley was a field assistant in the same department.

#### Redirect Examination

By Mr. Cohn:

Q. Do you know where either of those men are now?

A. No. Mr. Clendenin was retired on permanent and total disability a number of years ago, about 15 years back. Mr. Hensley left the Travelers ten or twelve years ago. I don't know what his connection is now.

Mr. Cohn: That is all.

Mr. Gerlack: That is all.

Mr. Cohn: That is the plaintiff's case.

Mr. Gerlack: That is the defendant's case.



CERTIFICATE OF REPORTER

I, Edward W. Lehner, Official Reporter, certify that the foregoing . . . pages is a true and correct transcript of all matter therein contained as reported to me and thereafter reduced to typewriting.

/s/ EDWARD W. LEHNER. [60]

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[Endorsed]: No. 11917. United States Circuit Court of Appeals for the Ninth Circuit. George H. Richardson, Appellant, vs. The Travelers Insurance Company, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Northern District of California, Southern Division.

Filed April 30, 1948.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the Circuit Court of Appeals for the  
Ninth Circuit

No. 11917

GEORGE H. RICHARDSON,

Appellant,

vs.

THE TRAVELERS INSURANCE COMPANY,

Appellee.

STATEMENT OF POINTS ON WHICH AP-  
PELLANT INTENDS TO RELY ON AP-  
PEAL AND DESIGNATION OF PARTS OF  
RECORD APPELLANT THINKS NECES-  
SARY FOR CONSIDERATION THEREOF  
(RULE 19, SUBD. 6-CCA-9TH)

Pursuant to the above rule, appellant states the following points on which he intends to rely on appeal, as follows:

1—The said District Court erred in finding that the appellee was not guilty of laches in instituting this present action in 1946 when it had the clear opportunity, in 1926 when it issued the policy, and again in 1928, again in 1931, again in 1933 and again in 1936 when it had the policy in its hands at its San Francisco branch and home offices, on each of these occasions in connection with policy loans, to discover the now claimed error in the issuance of the policy, and knew, or by the exercise of ordinary diligence, would have known of such error if any, but nevertheless waited some 19 years, after the issuance of the policy, and after appellant had

paid to appellee all of the 20 annual premiums called for under the policy, before instituting this present action to now reform the policy.

2—The District Court erred in finding and concluding that the California Statute of Limitations, Code of Civil Procedure, Sections 312 and 338, did not apply to the instant action.

3—That the District Court erred in finding that the “incontestable clause” of the policy did not apply to the present suit in the instant case.

4—The District Court erred in finding that the appellee only discovered for the first time the claimed error in the policy in 1946. In view of the District Court’s findings XVI that the appellee had the policy in his possession four times, namely July and August, 1928; September and October, 1931; October and November, 1933, and June, 1936, the said District Court’s findings are inconsistent and contradictory in the following respects, to wit:

Finding XVI finds the appellee had the insurance policy in question in its possession in its San Francisco branch and also in its Home Office in Hartford, Connecticut, in connection with policy loans four different times, namely, 1928, 1931, 1933 and 1936, whereas finding XVI also finds that the appellee discovered the claimed mistake in the issuance of the policy for the first time in March, 1946, and the said District Court erred in rendering judgment for the appellee based upon such inconsistent and contradictory findings.

5—The District Court erred in ordering judgment for the appellee in view of the appellee’s ad-

mitted examination of the policy in question in July and August, 1928; September and October, 1931; October and November, 1933, and June, 1936, and the Trial Court's finding XVI to that effect, and what appellant claims is a clear, unmistakable and inexcusable case of laches on the part of the appellee.

6—The District Court erred in finding that the appellant was not prejudiced by the appellee waiting 19 years and collecting all of the 20 annual premiums due under the policy and further waiting until the appellant was almost 65 years of age and obviously uninsurable before bringing the present action.

7—The District Court erred in finding that the policy of insurance was issued through mutual mistake of parties hereto and/or that the policy was issued by mistake of appellee which appellant at the time knew or suspected, and also in finding that the policy as issued was not the policy applied for by the appellant, and in finding that the special privileges inserted in the policy by the appellee was by mutual mistake of the parties and/or by mistake of the appellee which appellant at the time knew or suspected.

And also pursuant to said rule above mentioned, appellant hereby designates the following parts of the record he thinks necessary for consideration thereof, namely:

1—The complaint of Plaintiff but with the exhibits (photostatic copies thereof) printed or bound in 10 copies only of the printed record.



2—The answer and counterclaim of the Defendant, but with exhibits (photostatic copies thereof) printed or bound in 10 copies only of the printed record.

3—The answer of Plaintiff to Defendant's counterclaim.

4—The findings of fact and conclusions of law made by the court.

5—Judgment of the Trial Court.

6—Notice of Appeal.

7—Designation of Contents of Record on Appeal.

8—Statements of points on which Appellant intends to rely on appeal.

9—This Statement of Points on which Appellant intends to rely on appeal and designation of parts of the record Appellant thinks necessary for consideration thereof.

Dated: May 4, 1948.

/s/ ALVIN GERLACK,

Attorney for Appellant.

Receipt of a copy of the within Statement is hereby admitted this 4th day of May, 1948.

/s/ JOSEPH T. O'CONNOR,

/s/ HAROLD H. COHN,

Attorneys for Appellee.

[Endorsed]: Filed May 4, 1948.



No. 11,917

IN THE  
United States  
Court of Appeals  
For the Ninth Circuit

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GEORGE H. RICHARDSON,

*Appellant,*

VS.

THE TRAVELERS INSURANCE COMPANY,

*Appellee.*

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Brief for the Appellant

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FILED

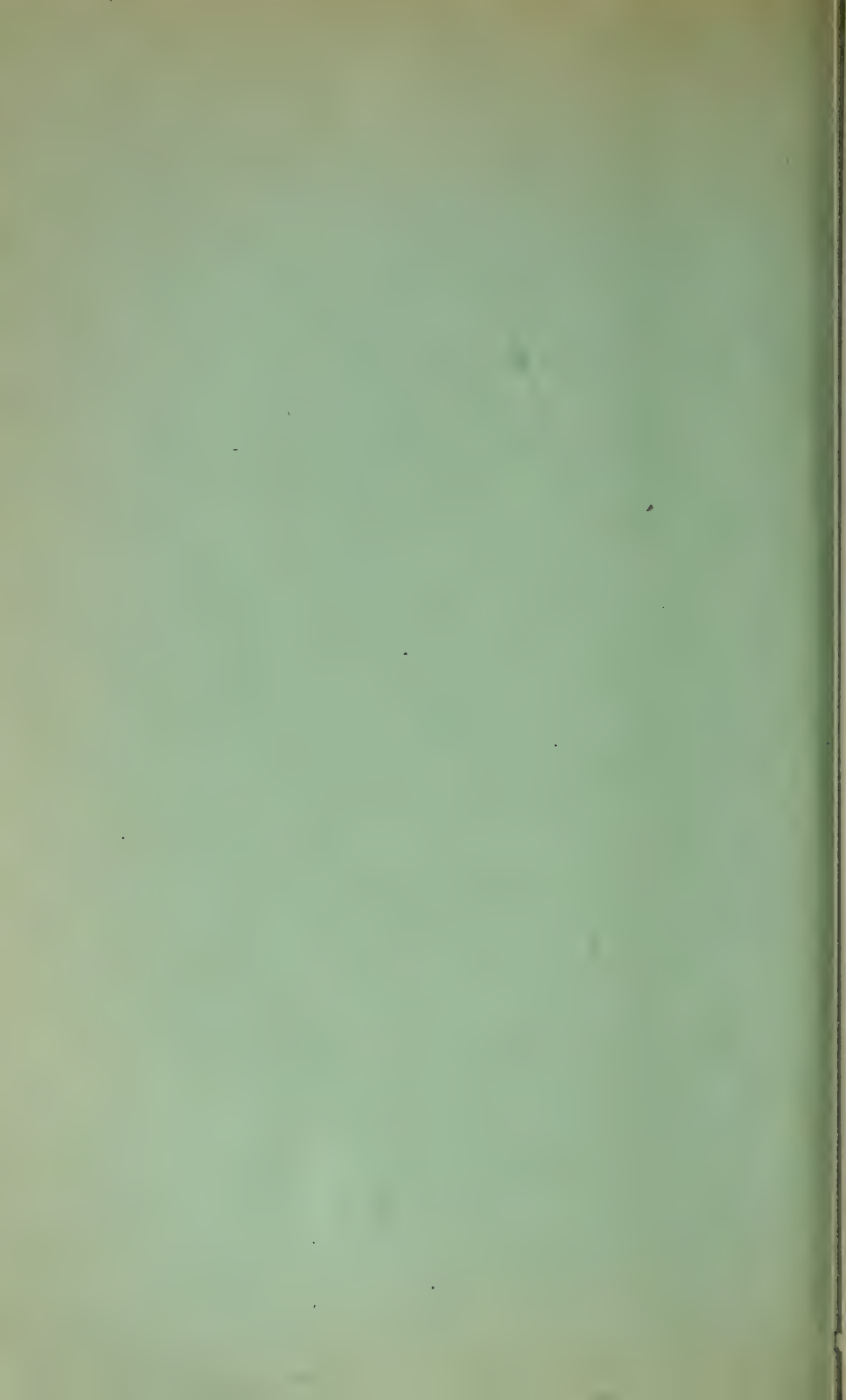
SEP 20 1948

PAUL P. O'BRIEN,

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## Subject Index

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	Page
Jurisdiction .....	1
Statement of the Case.....	2
The Four Policy Loans—Policy Back at Home Office Each Time .....	5
Questions Presented .....	5
Statement of Points .....	6
The “Incontestable Clause” .....	6
Argument .....	7
The Present Action Is Barred by Laches.....	7
The Insured Was Prejudiced.....	16
The California Statute of Limitations (C.C.P. Secs. 312 and 338) Applies by Analogy.....	16
The Incontestable Clause Does Apply.....	16
The Right to “Reform” the Policy Is Not Excepted in the Incontestable Clause of the Present Policy.....	20
The Trial Court’s Opinion.....	25
Conclusion .....	27

# Table of Authorities Cited

## CASES

	Pages
Austin, Mutual Reserve Fund v., 142 Fed. 398, 6 L.R.A. (M.S.) 1064 .....	17
Bernier v. Pac. Mut. Life Ins. Co. (Louisiana), 139 So. 629 .....	17
Black, Columbia Nat'l Life Ins. Co. v., 35 Fed. (2d) 571 (C.C.A. 10th) .....	24, 26
Boettcher, Kelly v., 85 Fed. 55, 62 .....	7, 16
California Life Ins. Co., Narber v., 211 Cal. 176 .....	19
Calvert v. Stoner, 84 A.C.A. 228 (Calif. Dist. Ct. of Appeals) .....	9
Chun Ngit Ngan v. Prudential Insurance Co., 9 Fed. (2d) 340, 341 .....	24
Columbia Nat'l Life Ins. Co. v. Black, 35 Fed. (2d) 571 (C.C.A. 10th) .....	24, 26
Dibble v. Reliance Life Ins. Co., 170 Cal. 199 .....	18, 19, 20
Dutton v. Prudential Ins. Co., 193 S.W. (2d) 938 .....	13, 15, 23
Hayes v. Travelers Ins. Co., 93 Fed. (2d) 568 (C.C.A. 10th) .....	11, 13, 14, 16
Kaufman v. New York Life Ins. Co. (Penna), 315 Pa. 34, 172 Atl. 306 .....	15, 16, 26
Kelly v. Boettcher, 85 Fed. 55, 62 .....	7, 16
Metropolitan Life Ins. Co. v. Asofsky (D.C. N.J.), 38 Fed. Supp. 464 .....	12
Metropolitan Life Ins. Co., Yablon v., 38 S.E. (2d) 534 .....	9, 15, 16
Mutual Benefit Assn., Wright v., 118 N.Y. 237, 16 Am. St. Rep. 749, 23 N.E. 186 .....	21
Mutual Reserve Fund v. Austin, 142 Fed. 398, 6 L.R.A. (N.S.) 1064 .....	17
Narber v. California Life Ins. Co., 211 Cal. 176 .....	19
Natl. Union Fire Ins. Co., v. John Spry Lumber Co., 235 Ill. 98, 85 N.E. 256, 259 .....	11
New York Life Ins. Co., Kaufman v., (Penna.), 172 Atl. 306 .....	15, 16, 26

	Pages
Prudential Ins. Co., Dutton v., (Missouri), 193 S.W. (2d) 938 .....	13, 15, 23
Reliance Life Ins. Co., Dibble v., 170 Cal. 199.....	18, 19, 20
Reliance Life Ins. Co. v. Thayer, 84 Okla. 238, 203 Pac. 190, 192 .....	22
Stoner, Calvert v., 84 A.C.A. 228.....	9
Thayer, Reliance Life Ins. Co. v., 84 Okla. 238, 203 Pac. 190, 192 .....	22
Travelers Ins. Co., Hayes v., 93 Fed. (2d) 568.....	11, 13, 14, 16
Upton, Assignee v. Tribilcock, 91 U.S. 45, 50 L.Ed. 203.....	11
Wagner v. Natl. Life Insurance Co. (C.C.A. 6th), 90 Fed. 395, 407 .....	11
Whitney Co. v. Johnson (C.C.A. 9th), 14 Fed. (2d) 24, 25.....	11
Wright v. Mutual Benefit Assn, 118 N.Y. 237, 16 Am. St. Rep. 749, 6 L.R.A. 731, 23 N.E. 186.....	21
Yablon v. Metropolitan Life Ins. Co., 38 S.E. (2d) 534.....	9, 15, 16

## STATUTES

California Statutes of 1923, Ch. 355, p. 731, amending Policies Code, Sec. 633.....	4
Civil Code #1668 .....	18
Civil Code #3527 .....	10
Code of Civil Procedure #312 and #338.....	5, 7, 8, 16
“Conformity Act” (28 U.S. Code #724).....	16
32 Corpus Juris., p. 1142, Sec. 249 (44 C.J.S., Insurance, Sec. 279) .....	10, 11
Federal Rules of Civil Proceeding Rules 43a and 81.....	16
Judicial Code, Sec. 24, Sec. 128.....	2





IN THE  
United States  
Court of Appeals  
For the Ninth Circuit

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GEORGE H. RICHARDSON,

*Appellant,*

VS.

THE TRAVELERS INSURANCE COMPANY,

*Appellee.*

---

**Brief for the Appellant**

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**JURISDICTION**

This is a suit for reformation of a contract of insurance issued by appellee, The Travelers Insurance Company, a Connecticut corporation, to appellant, a citizen of California, more than twenty years ago.

The jurisdiction of this Court and of the District Court have been properly invoked under Judicial Code, Sec. 24 (28 U.S.C.A. #41), and Judicial Code, Sec. 128 (28 U.S.C.A. #225). Judgment was entered in the District Court in favor of the plaintiff (appellee) on February 26, 1948 (R70). Notice of Appeal was filed March 26, 1948 (R70).

### STATEMENT OF THE CASE

George H. Richardson, the appellant, took out a \$15,000 life insurance policy (No. 373,735) on September 27, 1916, with annual premiums of \$309.75. On December 13, 1918, he took an additional policy (No. 482,573) for \$10,000 with annual premiums of \$232.40.

Both of these policies, aggregating \$25,000, were in full force with the appellee insurance company on December 31, 1926, when appellant, after certain conversations with appellee's officers (R119), dropped the 1918 \$10,000 policy No. 482,573, and reduced the 1916 \$15,000 policy No. 373,735 to a \$10,000 policy with special privileges, bearing the same number (#373,735). The premiums on the reduced 1926 \$10,000 policy were \$335.60 annually, of which \$48.10 was for total permanent disability. Disregarding the \$48.10 disability premium, the life insurance rate on the \$15,000 1916 policy was \$20.35 per \$1,000 of insurance, while on the 1926 \$10,000 policy the rate was \$28.57 per \$1,000—an increase of \$8.40 per \$1,000 of insurance. Both rates were based upon the insured's age in 1916, when the original policy (No. 373,735) was issued.

The application for the 1926 policy was for "\$10,000 Ins. Annuity, Age 65 on the Uniform Premium Plan with No. A Disability Provision." Appellee claims that by mis-

take of its officers and scriveners at its home office in Hartford, Connecticut, it issued to appellant its "\$10,000 Pension Policy, Age 65" instead. The policy was signed by appellee's President and also by its Assistant Department Secretary (R32).

The only essential difference between its "\$10,000 Ins. Annuity, Age 65" policy and its "\$10,000 Pension Policy, Age 65" appears to be the figures "\$500" in the "Pension" policy (R33) and "\$1,000" in its "Annuity" policy (R15). The precise language reading:

*"Options Available at Age 65.* The insured may select in lieu of all other benefits hereunder, one of the following options to become available upon the surrender of this contract at its anniversary when the insured shall have reached the age of 65, the amount of these options being stated for each \$500 of insurance" etc. (so-called "\$10,000 Pension Policy, Age 65") and "for each \$1,000 of insurance" etc., (for the so-called "\$10,000 Ins. Annuity, Age 65" policy. (Italics ours.)

There is nothing in the record to show that appellant knew or ever heard of these technical insurance terms prior to the trial of this action, although appellee claims its Life Insurance Rate Manual in force in 1916 (but used in rewriting the 1926 policy) does actually contain such terms. Appellee claims its 1916 Manual rate premium for the "\$10,000 Pension Policy, Age 65" was \$467.50 per year and \$287.50 per annum for its "\$10,000 Ins. Annuity, Age 65" policy.

Appellant, in the summer of 1926, became an insurance agent of appellee, soliciting accident policy sales exclusively (R114). He received "on the job" training only

(R116). This training did not include any instruction on how to use the life rate manual (R117). He received no training in life insurance (R103). He received no salary or drawing account but was paid a straight commission of 25% of the premiums for each accident insurance policy he sold (R114-115).

As the California law then read, it was necessary for anyone soliciting or selling any kind of insurance including accident insurance policies, to have an insurance agents license. These licenses were issued upon request of the particular insurance company employing the agent. Such licenses at that time permitted the agent to represent any insurance or surety company and to solicit and sell any and all kinds and types of policies—fire, automobile, life, health, accident, disability, marine, surety, etc., etc. Also no professional examinations, as such were required or given the applicant, although he had to be vouched for by the insurance company for which he was employed (Calif. Statutes 1923, Chapter 355, page 731, Amending Calif. Political Code, Sec. 633).

Appellant's efforts to sell appellee's accident insurance policies were not very successful, and after a few months appellant quit actively to represent appellee and returned to his former line of business, going in business for himself, in the early part of 1927 (R117-118). Although he did not formally resign as appellee's agent until December 31, 1927, nevertheless he was giving practically all of his time to his own business (R118). Apparently, he was not the type that makes a real success of the insurance business (R118).

There is no evidence in the record that appellant ever wrote any life insurance policies for appellee while acting



as its agent prior to the issuance of the instant policy on December 31, 1926, although almost two years later (R103) and long after he had formally resigned as appellee's agent, appellant wrote a couple of life insurance policies on his own life (R103-104).

#### **The Four Policy Loans—Policy Back at Home Office Each Time.**

After the issuance of the present policy on December 31, 1926, appellant, in July, 1928, delivered the policy into the hands of appellee at its San Francisco Branch Office for the purpose of negotiating a further loan on it. The policy was then sent by the San Francisco Branch Office to appellee's home office at Hartford, Connecticut. After being in the home office for about a month, it was returned to appellant in August, 1928 (R55). In a similar manner and for the same purpose, the policy was back at appellee's home office again for about a month in September and October, 1931 (R56) and similarly, again in October and November, 1933 (R56), and similarly, again in June, 1936 (R56) (Finding XVI-R55-56).

The "Special Privileges" clauses (which form the basis of this litigation) and the "Cash and Loan Values, Paid-up and Automatic Term Insurance" tables, which appellee presumably used on all four occasions in making said loans, are both found on the same (second) page of the policy (R33).

#### **QUESTIONS PRESENTED**

1. Is the appellee estopped by laches from maintaining this action?
2. Does the California Statute of Limitations (Code of Civil Procedure, Sections 312 and 338) apply by analogy



and bar the bringing of the present action on the policy? and,

3. Does the "Incontestable Clause" of the policy apply to and bar the present suit brought for the first time almost 20 years after its issuance, to reform the policy and pay only half the benefits called for in the policy, as issued?

### **STATEMENT OF POINTS**

(R. 132-133-134)

The District Court erred in:

1. Finding that appellee was not guilty of laches.
2. Finding that the California Statute of Limitations did not apply.
3. Finding that the "Incontestable Clause" did not apply.
4. Finding that appellee only "discovered" the claimed error for the first time in 1946.
5. Ordering judgment for appellee, after finding that appellee had the policy in its possession, four different times namely in 1928, 1931, 1933 and again in 1936, but only "discovered" the claimed error in 1946.
6. Finding that appellant was not prejudiced by this action to reform the policy brought almost 20 years after its issuance, after appellant had paid to appellee all 20 of the annual premiums demanded, and appellant was virtually 65 years of age and obviously uninsurable, and
7. The policy was issued through mutual mistake of the parties.

### **THE "INCONTESTABLE CLAUSE"**

Pleaded as an affirmative defense in our answer and counterclaim (R27) reads as follows:

“*Incontestability*. This contract shall be incontestable after one year from date of issue, except for non-payment of premiums \* \* \*

\* \* \* This contract is subject to the privileges and conditions recited on the subsequent pages hereof” (R27, 7).

### ARGUMENT

#### The Present Action Is Barred by Laches.

Under the settled rule, this present action to “reform” the policy 20 years later is now barred by laches. The established rule is well stated by Mr. Circuit Judge Sanborn in *Kelly v. Boettcher*, 85 Fed. 55, where, at page 62, it is said:

“When a suit is brought within the time fixed by the analogous statute, the burden is on the defendant to show, either from the face of the bill or by his answer, that extraordinary circumstances exist which require the application of the doctrine of laches; and, when such a suit is brought, after the statutory time has elapsed, the burden is on the complainant to show, by suitable averments in his bill, that it would be inequitable to apply it to his case. The cases of *Wagner v. Baird*, 7 How. 234; *Godden v. Rummell*, 99 U.S. 201; *Wood v. Carpenter*, 101 U.S. 135, 139; and *Rugan v. Sabin*, 10 U.S. App. 519, 3 C.C.A. 578, 582 and 53 Fed. 415, 420, belong to the class of cases in which the doctrine of laches was applied after the statute of limitations had run.”

The “analogous statute,” pleaded in our answer (R26) is found in Sections No. 312 and No. 338, of the Code of Civil Procedure of the State of California, the applicable parts of which read as follows:

Sec. # 312. "*Civil Actions*—Civil Actions, without exception, can only be commenced within the periods prescribed in this title, after the cause of action shall have accrued," and

Sec. #338. "*Three Years \* \* \* Fraud and Mistake Within Three Years:*

\* \* \* 4. An action for relief on the ground of fraud or mistake. The cause of action in such case not to be deemed to have accrued until the discovery, by the aggrieved party, of the facts constituting the fraud or mistake."

The trial court in Findings XVI (R55) states that appellee's first knowledge of the claimed error was in March 1946, notwithstanding that in said Finding the Court also finds that appellee had the policy in its possession in 1926, 1928, 1931, 1933 and again in 1936. The "loan values" which the company presumably used in making said loans are found on the lower half of the same page (page 2) of the policy which contains the "special privileges" which appellee now contends were issued by mistake. A corporation, of course, can only act through its servants and agents. On each of the four occasions when the policy was submitted to appellee by appellant in connection with these loans, had the Company's servants who read the "loan values" raised their eyes to the upper half of the same page, they would have discovered the now claimed error.

That the appellee, after being guilty of such undeniable, unexplained and repeated acts of negligence, should now be allowed to profit by its unquestioned acts of carelessness and omission, presents an untenable theory of law and fact that should receive no consideration in this

court. We submit the trial court's findings in this respect are contrary to the admitted facts in the case, and find no support in the evidence.

"Where there are irreconcilable findings upon a material issue, an appellate court can do nothing but reverse."

*Calvert v. Stoner*, 84 A.C.A. 228 (Calif. Dist. Ct. of appeals).

The admitted facts clearly show that appellee knew or should have known as early as 1928, but certainly as late as 1936, that such mistake, if any, was made. Waiting thereafter 10 years before asserting such claimed error is unreasonable. It should now be held by this court that the California Statute began to run at least in 1936 when the company made the fourth loan on the policy. For obviously means of discovery is equivalent to discovery.

The facts in *Yablon v. Metropolitan Ins. Co.*, 200 Georgia 693, 38 S.E.(2d) 534, are strikingly similar to the facts in the case at bar. There the Supreme Court of Georgia, at page 543, said:

"Has the defendant been guilty of laches to the extent that it would now be inequitable to allow reformation? Unquestionably the evidence did not justify the direction of a verdict that the company had been so guilty. The record shows that the defendant has waited from November 6, 1922, to February 11, 1942, to assert its right for such equitable relief. In the meantime, it has collected all of the premiums fixed by it as due, and frequently has had actual possession of the policy, with ample opportunity to examine it; the insured has grown old and become totally disabled, making it now impossible for him



to secure the type of insurance which he insists that he requested."

and again, on page 544, the same court said:

"It was not shown by any evidence that the insured had any knowledge of or connived in any way with the insurer for the stated premium rate in the rider, providing that payment for total and permanent disability would be lower than the prescribed rate applicable to other persons. In the absence of such showing, we do not think that the insurer, approximately 19 years after the issuance and delivery of the policy and rider, and on its action to reform the contract for alleged mistake, could lawfully contend that it was not liable because the rate of premium which the company inserted in the face of the rider was lower than its rate-book schedule for such protection, and because this would be a discrimination. The defendant will not now be allowed to benefit by its own wrong, in which the plaintiff was not likewise a wrongdoer."

Section #3527 of the Civil Code of California provides:

"The law helps the vigilant before those who sleep on their rights."

That it is the duty of one executing a contract to read it, is, of course, elementary. In 32 Corpus Juris, p. 1142, Sec. 249, 44 C.J.S., Insurance, Sec. 279, it is stated:

"A court of equity usually will not reform a policy in order to relieve a party from a mistake which was the result of his own negligence." See also *Yablon v. Metropolitan Life Insurance Co.*, supra, and cases cited; and it has even been held that the wrongful conduct of a scrivener, who did not write the con-



tract as instructed, will not relieve the party who directed its preparation, but who failed, through his own negligence, to read it before sending it to the other party, who in good faith accepted it and acted upon it. *Newsome v. Harrell*, 146 Ga. 139, 147; 90 S.E. 855."

"The company is bound to know the provisions of its own policy, and must move promptly in order to obtain a correction."

32 Corpus Juris 1142.

"Those who suffer in consequence of their own culpable inertness are without remedy."

*Natl. Union Fire Ins. Co. v. John Spry Lumber Co.*,  
235 Ill. 98, 85 N.E. 256, 259.

If there was a mistake, as appellee claims, had the officers of appellee read the policy, it is reasonable to suppose they would have discovered the error, if not in 1926, then in 1928, 1931, 1933 or 1936. And if one signs a written contract without acquainting himself of its contents, he is estopped by his own negligence to ask relief from his own obligation, if there is no fraud or artifice in procuring his signature, or, putting it another way, one having the capacity and opportunity to read a contract who executes it without reading it, in the absence of fraud or imposition or special circumstances excusing his failure to read it, is charged with knowledge of its contents and cannot avoid the contract by asserting that it did not express what he intended. See *Upton, Assignee v. Tribilcock*, 91 U.S. 45, 50 L. Ed. 203; *Whitney Co. v. Johnson* (C.C.A. 9th) 14 Fed.(2d) 24, 25; *Hayes v. Travelers Ins. Co.*, 93 Fed.(2d) 568, 570 (C.C.A. 10th); *Wagner v. Natl. Life Insurance Co.* (C.C.A. 6th) 90 Fed. 395, 407.

In *Metropolitan Life Ins. Co. v. Asofsky*, (D.C. N.J.) 38 Fed. Supp. 464, it was held that the insurer's failure to check premiums stated in the policy or by other means to discover its error during two months and ten days before delivery of the policy to insured prevented the insurer from having policy reformed.

We think this rule should apply to and be equally binding upon an insurance company and a policyholder alike.

There is in the instant case no claim or suggestion that the appellant Richardson practiced any fraud or artifice, either in connection with the original issuance of the policy, or in connection with any of the four policy loans when the policy was back at appellee's home office. Likewise it is not claimed by appellee that appellant had any knowledge of or connived in any way with the appellee insured for the stated premium rate on the rewritten 1926 policy. In the absence of such showing we do not think that the appellee insurer in its present action to now "reform" the contract, can lawfully and reasonably contend that it is not liable because the rate of premium which the company inscribed in the face of the policy was lower than its 1916 rate-book schedule for such protection. We feel the appellee should not now, at this late date, be allowed to benefit (by collecting all the premiums) from its own wrong in which the appellant was admittedly not likewise a wrongdoer.

The burden of proving and establishing a mutual mistake, or the mistake of appellee coupled with fraud or inequitable conduct on the part of appellant, was clearly on appellee. This burden must be met by establishing it by evidence of the clearest, unmistakable and most satisfactory character. A mere preponderance of the evidence

is not sufficient to satisfy the burden of proof. The evidence must establish the proof virtually beyond a reasonable doubt. See *Hayes v. Travelers Ins. Co.*, supra, and other cases therein cited.

In *Dutton v. Prudential Ins. Co.*, (Mo.) 193 S.W.(2d) 938 the Supreme Court of Missouri, at page 943, says:

“It has been held by our courts in many cases that to justify the reformation of such an instrument as we have before us (insurance policy), on the ground of mutual mistake, the evidence of such mutual mistake must be ‘so clear, convincing and complete as to exclude all reasonable doubt in the chancellor’s mind,’ and that ‘a mere preponderance of the evidence is not sufficient.’ Furthermore, courts of equity do not grant reformation on ‘probability’ or even the mere preponderance of the evidence, but only on ‘certainty of error.’ *Employers’ Indemnity Corporation v. Garrett, et al.*, 327 Mo. 874, 38 S.W.(2d), 1049, 1055; *Stubblefield v. Husband*, 341 Mo. 38, 105, S.W.(2d) 419.”

The policy here was executed by the President and Assistant Department Secretary of appellee Insurance Company. Appellee claims, and the trial court found that the policy as written provides for cash benefits at age of 65, of \$1,083, per \$500 of insurance, instead of \$1,083 per \$1,000 of insurance.

Although the trial court, in its “Opinion and Order” (R41), says that plaintiff alleges, and the court finds, that it erroneously selected the wrong printed form of policy, etc., there is not even a scintilla of evidence to this effect in the record. There is nothing more than an implication that the premium stated in the policy as issued was not

according to the 1916 rate manual. We search the record in vain for even a suggestion as to why or under what circumstances the mistake, if it was indeed a mistake, actually occurred. There is no substantial evidence in the record that the wrong printed form of policy was selected, no substantial evidence that a scrivener actually made a mistake. We submit that the implications and inferences to this effect are at best but weak suggestions that the Company might have wished to issue another type of policy. No explanation as to just how this "mistake" came about, if such it was.

Certainly this does not meet the burden of proof and constitute the "clear and unmistakable" evidence required to establish reformation of an insurance policy, especially after the maturity of the policy, when after a lapse of 20 years, the insured had become 65 years of age and obviously uninsurable and after the insured has performed all of his part of the insurance bargain.

Frankly, we do not think there was any mutual or other mistake in issuing the policy, but refrain from arguing the point only in view of the adverse findings of the trial court.

But even assuming, without admitting, that there was a mistake, the insurer should not at this late date be allowed to come into court, and now seek to be relieved from the natural consequences of its own negligent acts in not discovering what it now contends is an obvious error in the policy. No mistake on the part of the insured has been shown and the plaintiff insurer has not even charged the insured with any fraud in connection with the transaction. See *Hayes v. Travelers Insurance Co.*, supra;



*Dutton v. Prudential Ins. Co.*, supra; and *Yablon v. Metropolitan Life Ins. Co.*, supra, quoted above.

In *Kaufman v. New York Life Insurance Co.*, 315 Pa. 34, 172 Atl. 306, the mistake was even more pronounced than in the present instance. There, the insurance company also claimed that it made a mistake in issuing the policy. The facts are quite similar to the facts in the case at bar. The court there denied reformation upon much stronger evidence than appellee here produced in the trial court.

In the instant case there was definitely no mutual mistake of the parties. It is our contention that the policy was issued by one party in accordance with the understanding of the other party. If a mistake did actually occur, it was at most unilateral on the part of the insurer and was its own negligent fault. Had the insurer company in 1928 (a year and a half after it rewrote the insured's policy) exercised even the slightest care and diligence in reading the upper half of page 2 of the policy, and discovered then what it now claims is an obvious error, it could have then notified the insured and this lawsuit would never have been necessary. At any rate, a mistake, if made by the insurer, does not bind this innocent insured as the above quoted cases clearly show.

Appellee admits and the trial court so found that appellee kept no copy of this insurance contract which it entered into with appellant (R81, Finding VI—R52). In this day and age of widespread and inexpensive photostatic copying of documents, it is earnestly submitted this, in itself, constitutes a circumstance of negligence on the part of appellee.



### **The Insured Was Prejudiced.**

The prejudice to the insured, we think, is so obvious as to call for little more than a mere statement of the facts as set forth above. Where an insured who is now 65 years of age and obviously uninsurable, as a result of conversations had with an official of the insurer, drops \$25,000 of life insurance protection to take out the present policy—certainly he will have been prejudiced and harmed if the insurer here is now allowed to prevail in its present contention. See *Yablon v. Metropolitan Life Ins. Co.*, supra; *Hayes v. Travelers Ins. Co.*, supra; *Kaufman v. New York Life Insurance Co.*, supra.

### **The California Statute of Limitations (C.C.P. Secs. 312 and 338) Applies by Analogy.**

Under the "Conformity Act" (28 U.S. Code #724) and Rule 43A and Rule 81 of the Federal Rules of Civil Procedure, and the decisions construing the same, the Federal Courts normally apply the State Statutes and the decisions in the States where the Federal Courts sit. This applies to equity cases as pointed out above. See *Kelly v. Boettcher*, supra; *Wagner v. Baird*, supra; *Godden v. Rummell*, supra; *Wood v. Carpenter*, supra; *Rugan v. Sabin*, supra, cited above. See page 7 of this brief.

### **The Incontestable Clause Does Apply.**

The incontestability clause in the policy reads as follows:

*"Incontestability.* This contract shall be incontestable after one year from date of issue, except for non-payment of premiums. It is free from conditions as to residence, occupation, travel or place of death. No permit or extra premium will be required for

military or naval service in time of war or in time of peace.

“This contract is subject to the privileges and conditions recited on the subsequent pages hereof.”

We can think of no better or more logical application of the incontestability clause of an insurance policy than in the present instance. For had the insurer company within a reasonable time after writing the policy or within a reasonable time after discovering this alleged “mistake,” in 1928 or 1931 or 1933 or 1936, notified the insured, he could then at his age at that time have taken out other insurance or have been reinstated in his former \$25,000 policies. For certainly, incontestable clauses in insurance policies must have been intended to be something more than mere “bait” to entrap credulous, naive and unwary buyers of life insurance. The history of such clauses is well known.

It has been said that the incontestable clause may properly be regarded as a most important, if not *the most* important, provision in a life insurance policy. While each part of a life insurance policy is of course important, and has its function, the incontestable clause has its influence over the other portions of the policy.

The courts have said that where a policy contains such a clause, it is, in effect, one kind of a policy, before the expiration of the contestable period, and a different and more valuable policy thereafter.

See:

*Bernier v. Pac. Mut. Life Ins. Co.*, (Louisiana) 139 So. 629;

*Mutual Reserve Fund v. Austin*, 142 Fed. 398, 6 L.R.A. N.S. 1064.

The general and almost universal rule in the United States is laid down in *Dibble v. Reliance Life Ins. Co.*, 170 Cal. 199. This case has now become one of the leading cases in the country and has been widely cited by State and Federal Courts.

The rule as there stated by the Supreme Court of California, per Mr. Chief Justice Angelotti, is that an incontestable clause (after expiration of the contestable period) bars and precludes *every* defense to or any contest of the policy on any ground which is not specifically reserved or excepted in the incontestable clause itself.

In that case the company defended on the grounds that there were false statements or representations in the application for the policy, and filed a cross-complaint, seeking cancellation of the policy. The insured contended that such defense was barred by the incontestable clause in the policy. The company, at the same time, contended that for the court to so hold would be against public policy, and in violation of the provisions of section 1668 of the Civil Code, as exempting the insured from responsibility for his own fraud. The Supreme Court followed the general rule hereinbefore set out, and held that fraud as a defense was barred by the incontestable clause, and that to so hold would not violate public policy, as condoning fraud, but, on the contrary, it recognizes fraud and all other defenses, by providing ample time and opportunity within which they may, and after which they may not be asserted.

The court stated that incontestable clauses are in the nature of and serve a similar purpose as statutes of limitation and repose, and that the parties to a contract may provide for a shorter limitation than that fixed by

law, and that such an agreement is in accord with the policy of statutes of that character. The court further made reference to and invoked the well-settled rule that in construing the provisions of a policy, all doubts and ambiguities must be resolved against the insurance company.

See:

*Narber v. California Life Ins. Co.*, 211 Cal. 176.

Attention is invited to the first sentence of the clause, namely: "This *contract* shall be incontestable after one year from date of issue (in this case December 31, 1926), except for non-payment of premiums," (italics ours), the *only* exception being the non-payment of premium. The plaintiff insurer admits in its complaint that all premiums have been paid.

In *Dibble v. Reliance Life Ins. Co.*, supra, the opinion, prepared originally by Mr. Justice Burnett of the California District Court of Appeal of the Third District and adopted in part by the California Supreme Court, it is said:

"It may be added that the subject is thoroughly considered in the note to *Clement v. New York Life Ins. Co.*, as reported in 42 L.R.A. 247, and I think the statement is justified that all the recent cases and authorities hold that where a reasonable time is given for investigation an incontestable clause is valid as against all defenses not excepted from its operation.

"And in this connection it may be said that I can find no warrant for the assertion that by the terms of the policy here *fraud* is withdrawn from the application of said provision.



“There is no contention that *fraud* is *expressly* excepted and I think there is no such implication. As I understand it, the clause in which the term is used simply implies that in case of fraud the statements made in the application shall be deemed *warranties*, but there is nothing to suggest that a defense on said ground is not barred by the lapse of the time period prescribed.”

**The Right to "Reform" the Policy Is Not Excepted in the Incontestable Clause of the Present Policy.**

Certainly, it must necessarily follow that if an insurance company can waive and except itself from the defense of gross fraud on the part of the *insured*, it should be able to correspondingly waive and except itself from defending suit on the policy (our counterclaim) based upon its own negligence. Especially where its defense and contest of one-half the policy involves a totally innocent policyholder who in good faith performed his part of this insurance bargain by paying *all* premiums in full.

Regarding the company's attempted defense and cross-complaint to cancel the policy, the Supreme Court of California, in *Dibble v. Reliance Life Ins. Co.*, *supra* (page 206) states:

“To hold otherwise would be to permit such a clause in its unqualified form to remain in a policy as a deceptive inducement to the insured.”

We respectfully submit that anyone who has ever been solicited to buy a life insurance policy, and mentioned to the agent, the possibility of lawsuits in connection with life insurance policies, can really appreciate just what the Court was referring to when it used the language above quoted.



Regarding the insurance company's defense that the insured was a trusted employee of the company, the court, at page 204, said:

“Nor can I see that the legal aspect of the situation is changed by the circumstance that the insured was a trusted employee of the company. As far as the policy itself is concerned, the parties sustained the same relation as in the ordinary case of life insurance. The company would certainly have the right to grant to its employees the same favor as to strangers and it should be bound by the same obligations. Indeed, as far as opportunity for inquiry and investigation to ascertain fraud is involved in the question, there is reason for holding the insurer to a stricter accountability where an employee is the insured.”

Mr. Chief Justice Angellotti, in his opinion, quotes from *Wright v. Mutual Benefit Assn*, 118 N.Y. 237, 16 Am. St. Rep. 749, 6 L.R.A. 731, 23 N.E. 186, as follows:

“It is not a stipulation absolutely to waive all defenses and to condone fraud. On the contrary, it recognizes fraud and all other defenses but it provides ample time and opportunity within which they may be, but beyond which they may not be, established. It is in the nature of and serves a similar purpose as statutes of limitations and repose, the wisdom of which is apparent to all reasonable minds. It is exemplified in the statute giving a certain period after the discovery of a fraud in which to apply for redress on account of it and in the law requiring prompt application after its discovery if one would be relieved from a contract infected with fraud. The parties to a contract may provide for a shorter limitation than that fixed by law and such an agreement is in accord with the policy of statutes of that character.”

In *Reliance Life Ins. Co. v. Thayer*, 84 Okla. 238, 203 Pac. 190, 192, the court, in passing on the validity of an incontestable clause, said:

“Webster’s International Dictionary defines these words as follows:

“‘Contest: Earnest struggle for superiority, defense, victory, etc.; competition; emulation; strife or argument.’”

In the present action under Webster’s definition, the appellee certainly is making a contest of the policy in resisting payment of the full amount stated in the policy.

The language of the policy is indeed clear and unmistakable—no ambiguity whatever exists—the policy on page 2 reading in part as follows:

“Options available at age 65. The insured may select in lieu of all other benefits hereunder one of the following options to become available upon the surrender of this contract at its anniversary when the insured shall have reached the age of 65, the amount of these options being stated for each \$500 of insurance.

1. Receive a cash payment of \$1,083.00.
2. Receive a cash payment of \$739.00 and a paid-up contract payable at death for \$500.00.
3. Receive a paid-up contract payable at death for \$1,574.00.
4. Receive an annual income of \$112.83 payable during the natural life of the insured.”

Appellee’s present action is clearly an “earnest struggle for superiority” in attempting to pay only one-half of the amount called for in the policy and its present action under the form of an action to “reform” the contract

of insurance, as well as its defense of our counterclaim, is undeniably a "defense" to our counterclaim; and for the same reason appellee's present action certainly is an "earnest struggle for victory"; also a "competition" with the appellant for one-half the amount plainly stated in the policy; its present action is clearly both "strife" and "argument" with the appellant over his right to recover the full amount stated in the policy. In other words appellee, in resisting payment of the full amount stated in the policy, comes clearly within Mr. Webster's definition above quoted. The limitation contracted for in the policy (incontestable clause) is one year. The year ended on December 31, 1927 and the company's right to reform the policy or otherwise resist payment of the amount clearly stated in the policy (except for non-payment of premiums), expired on that date. Its present action filed in August, 1946—18½ years after—comes too late.

The policy having been submitted to the appellee insured by appellant, on the four occasions when appellant secured loans on it, we think the fact that appellee made no effort to change the policy or correct any error in it, is strong evidence that it considered that no error existed. Commenting on a somewhat similar situation, the Supreme Court of Missouri, in *Dutton v. Prudential Ins. Co.*, supra, at page 944, says:

"The testimony of Mr. Haley that he saw the insured almost every week after the delivery of the policy and that the insured never at any time expressed any dissatisfaction with the policy, and did not make any claim of mistake in the policy, is strong proof that the insured did not believe there was any mutual mistake in the policy as written. Furthermore, the

fact that the insured accepted the policy and kept it for more than one year prior to his death without objection to any of its terms or conditions, gives rise to a presumption that the contract as written sets forth fully and correctly the true agreement of the parties" (citing authorities).

Indeed if appellant had in fact possessed the improper motive to gain more than he bargained for, evidently imputed to him by the trial court in its opinion, it seems to us highly improbable that he would have risked discovery by voluntarily submitting the policy to the company so soon (1928) after its issuance on December 31, 1926.

This court, per the late Mr. Circuit Judge Rudkin, one of the ablest and most distinguished judges ever to have sat upon the bench, in *Chun Ngit Ngan v. Prudential Ins. Co.*, 9 Fed. (2d) 340, 341, said:

"The overwhelming weight of authority supports the rule that the incontestible clause commonly found in life insurance policies is in effect a short period of limitations, and that a policy can only be contested within the meaning of the clause by proceedings in court to which the insurer and the insured or his representative or beneficiary are parties" (citing cases).

In *Columbia National Life Ins. Co. v. Black*, 35 Fed. (2d) 571 (C.C.A. 10th), it is held that the incontestable clause does not apply to a suit to reform an insurance policy. We submit that a careful reading of the opinion in that case discloses that the holding does violence to the plain wording of the language employed in the policy as well as violence to the ordinary and accepted mean-



ing of those words as defined by Webster and the courts. It is unnecessary to cite authorities to the effect that words in an insurance policy are to be given their ordinary and usual meaning, and in case of ambiguity, are to be construed against the insurer and in favor of the policy holder.

### **The Trial Court's Opinion.**

The trial court in his opinion uses almost the identical argument set forth in appellee's counsel's brief. By way of explanation as to why appellee did not "discover" the claimed error when it had the policy four times in its possession in 1928, 1931, 1933 and 1936 the opinion says:

"By way of explanation as to why plaintiff did not discover the error on the other times that the policy was in its possession, the testimony indicates that when the policies were received they were referred to a department of the plaintiff which checks merely upon the cash or loan value and registers the assignment for the purpose of the loan. It is shown that that department has no connection with the issuing department or the policy writing department and that the table of loan values was correct for the insurance annuity policy and that there was no occasion in making loans on the policy, to refer to the special provisions of the policy where the error was located."  
(R42, 43)

Yet further on in its opinion the court argues that appellant *must* have been cognizant of a mistake in the issuance of the policy, the court saying:

"It is incredible that defendant did not familiarize himself with the special privileges" (R45, 46) and  
"I am satisfied that he read these provisions and,



if he did read them he must have realized that a mistake had been made." (R46)

Just why such a high degree of knowledge of all phases of the insurance contract was expected of appellant and not of the appellee insurer, with its legions of technical insurance experts, we are unable to discern. At any rate the speculative inference that appellant *must* have read his policy at the time it was issued, certainly falls far short of constituting the "clear, convincing, and unmistakable evidence beyond a reasonable doubt" required to "reform" a policy of life insurance—especially 20 years after it was issued.

The distinguishing characteristics between *Columbia Natl. Life Ins. Co. v. Black*, supra, and the instant case is that in that case, the company within a relatively short time after the issuance of the policy wrote the insured and called attention to the mistake and demanded the policy be surrendered to it for correction. *But that is not this case*, where the appellee first demanded the policy be reformed in March, 1946, almost 20 years after its issuance and almost 19 years after the right to contest it had expired under the incontestable clause.

In *Kaufman v. New York Life Ins. Co.*, supra, the Supreme Court of Pennsylvania, beginning at page 307, distinguishes *Columbia Natl. Life Ins. Co. v. Black*, supra, and most of the other cases cited by counsel in his briefs in the lower court.

**CONCLUSION**

As appellee (1) failed to prove its right to a reformation of the policy by the "clear unmistakable and unequivocal evidence beyond a reasonable doubt" as required by the rule, and, (2) was guilty of inexcusable negligence and laches in not discovering the claimed error at least in 1936 after having previously had five clear opportunities to do so, and, (3) failed to bring the present action to reform within a reasonable time, and, (4) failed to bring the present action within the three years required by the California Statute of Limitations, and, (5) failed to bring the present action within the one year allowed by the policy to contest it, it is respectfully submitted that the judgment of the lower court should be reversed and judgment entered for appellant for the full amount stated in his policy.

Dated: San Francisco, California,  
September 20, 1948.

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*Attorney for Appellant.*



No. 11,917

IN THE

United States Court of Appeals  
For the Ninth Circuit

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GEORGE H. RICHARDSON,

*Appellant,*

VS.

THE TRAVELERS INSURANCE COMPANY,

*Appellee.*

BRIEF FOR APPELLEE.

---

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FILED

OCT 20 1945

PAUL P. O'BRIEN, &





## Subject Index

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	Page
Statement of case .....	1
The questions presented .....	7
Argument .....	7
I.	
Appellee's action was not barred by laches nor was the assured prejudiced .....	7
A. Laches .....	7
B. There was no prejudice to the insured .....	21
II.	
The present action is not barred by any statute of the State of California .....	22
III.	
The incontestable clause does not bar the present action.....	22
IV.	
The trial court's opinion .....	26
Conclusion .....	26

## Table of Authorities Cited

Cases	Pages
Berry v. Continental Life Insurance Co. (Mo.), 33 S. W. (2d) 1016, 224 Mo. App. 1207 .....	11
Brown v. Oxtoby, 45 Cal. App. (2d) 702 .....	8
Buck v. Equitable Life Insurance Society (Wash.), 165 Pac. 878, 96 Wash. 683 .....	11
Columbia National Life Insurance Co. v. Black, 35 Fed. (2d) 571 .....	9, 19, 20, 21, 23, 25
Dibble v. Reliance Life Insurance Co., 170 Cal. 199 .....	25
Dutton v. Prudential Insurance Co. (Mo.), 193 S. W. (2d) 938 .....	18
Hayes v. The Travelers Insurance Company, 93 Fed. (2d) 568	18
Kaufman v. New York Life Insurance Co. (Penn.), 172 Atl. 306 .....	18, 19
Long v. Long, 76 Cal. App. (2d) 716 .....	8
Mates v. Penna. Mutual Life Insurance Co. (Mass.), 55 N. E. (2d) 770 .....	24, 25
Metropolitan Life Insurance Company v. Asofsky, 38 Fed. Supp. 464 .....	16
New England Life Insurance Co. v. Jones, 1 Fed. Supp. 984	11
Prudential Insurance Co. of America v. Deane (Delaware), 27 Atl. (2d) 365 .....	10
Smetherhan v. Laundry Workers Union, 44 Cal. App. (2d) 131 .....	8
Yablon v. Metropolitan Life Insurance Co. (Ga.), 38 S. E. (2d) 534 .....	14, 18
Youngs v. Metropolitan Life Insurance Co., 28 Ohio NPNS 179 .....	11

## TABLE OF AUTHORITIES CITED

iii

### Codes

Page

California Code of Civil Procedure:

Section 338 ..... 22

Section 338, Subdivision 4 ..... 10

### Texts

Couch, Cyclopedia of Insurance Law, Section 392..... 15

On December 13, 1926, appellant was already insured in the Travelers Insurance Company under two policies of insurance, on which he was paying premiums exceeding \$500.00 a year. (R. 99; R. 111; R. 24-25.) On that date, he signed an application for an "Insurance Annuity, Age 65, on the Uniform Premium Plan". The principal amount of insurance was \$10,000.00. (Plaintiff's Exhibit "A", R. 5.) The premium on the policy applied for was the sum \$287.50 per year. (R. 83.) Appellant paid the further sum of forty-eight odd dollars for disability benefits, which are not material to this lawsuit and will not, therefore, be hereafter referred to.

The insurance annuity contract was based upon an insurance unit of \$1,000.00 and contained special privileges entitling assured, at age 65, to receive a cash payment of \$395.00 for each \$1,000.00 of insurance and a paid up contract, payable at death, for \$1,000.00. (R. 83-84; Exhibit C, R. 15.) *We repeat, this was the policy of insurance applied for.* The company also issued for a much higher premium, to wit: \$467.50 per year for \$10,000.00 worth of insurance, a policy known as its "Pension Policy, Age 65". This latter policy was based on an insurance unit of \$500.00 and contained a special privilege entitling the assured, at age 65, to receive \$739.00 for each \$500.00 of insurance and a paid up contract, payable at death, for \$500.00. (R. 84; Exhibit B, R. 7.)

Under the insurance annuity, also under the special privilege section, the insured was entitled to receive

for each \$1,000.00 of insurance, at age 65, in lieu of all other payments, a cash payment of \$1,083.00. Under the pension form policy, in lieu of all other payments, the insured was entitled to receive, at age 65, for each \$500.00 of insurance, a cash payment of \$1,083.00. (Exhibits B and C, R. 7-14.) Except for the difference hereinabove noted, and except for a difference in the loan value table, the two forms of policy for all practical purposes were, and are identical. (Exhibits B and C, *supra*).

Appellant did not receive the policy of insurance applied for, to wit: the annuity form policy. Instead, the policy writer, whose duty it was to issue the policy based upon appellant's application, through inadvertence and error, selected the wrong printed form and inserted in the policy actually delivered to appellant the special privilege called for by the pension form policy, including the erroneous insurance unit of \$500.00, instead of the special privileges called for by the annuity form policy with the correct and applied for insurance unit of \$1,000.00. In all other respects, including the loan value table, the policy delivered to appellant was the annuity form policy for which he applied and which the company intended to issue. (Answer and Counter Claim of Appellant, R. 31-33; R. 87-89.)

*Throughout the life of the contract, appellant paid the premium called for by the policy, to wit: the annuity premium, and not the higher pension premium. (R. 77.)*



Appellee kept no copies of policies issued by it to its insureds. The only thing kept by appellee is a master form of all the various contracts issued by it, a record of the assured's name, the type of policy which he has and the premium which he is to pay thereon. Nothing in the company's records would disclose the error made in issuing the wrong policy form to an assured. (R. 79-82).

Appellant had assigned the policy, which is the subject matter of this lawsuit, to the Crocker First National Bank of San Francisco. In March of 1946, the bank made inquiry of appellee as to the maturity value of appellant's policy and then, for the first time, the error was discovered. Prompt demand was made by appellee for surrender of the policy in order that the error might be corrected, which demand was refused and then this lawsuit immediately followed for the purpose of correcting the mistake made. (R. 91-93.)

Although the policy was in the hands of the company on several occasions after its issue for loan purposes, the error was not discovered on such occasions because the company's loan division has no connection with its issuing or policy writing division. The table of loan values was correct for the insurance annuity policy, the policy applied for by appellant, and there was no occasion in making loans on the policy to refer to the special privilege section of the policy where the error was located. (R. 93-94; R. 33.)

At the time of applying for the policy, appellant was a duly licensed life insurance agent under contract to appellee herein. (R. 98-99; Plaintiff's Exhibit 4.) On conflicting evidence, the trial court found that appellant had been given definite training with the life manuals of the company and on the subject of life insurance. (R. 109-110.)

At the time of applying for the policy which was issued, appellant was in difficult financial circumstances; he had loans on his pre-existing policies and was having difficulty in paying premiums thereon; he intended to surrender the policies for their cash value and perhaps take out a new one; he was paying in excess of \$500.00 per annum on premiums for the policies he then had and the switch to the policy involved herein would result in reducing the premium to \$287.50 per year, which was far more in line with appellant's ability to pay; the pension form policy was never discussed. (R. 106-109.)

Based upon the foregoing evidence, the trial court quite properly found that there was such a mistake in the issuance of the policy that appellee was entitled to the reformation it sought.

In his statement of the case, appellant states that he had conversations with appellee's *officers* before exchanging his insurance to its present form. The cited reference to the transcript fails to indicate that these persons were officers of the company; their status, and even their identity is much beclouded; but even if

such conversations did take place, they would be immaterial.

Appellant states that the record does not show that he knew or ever heard of these technical insurance terms, having reference apparently to the terms “\$10,000.00 pension policy” and “\$10,000.00 insurance annuity”. The trial court found to the exact contrary, based on the competent testimony of the witness Whitaker. (R. 109-110.) The trial court also found this to be so because appellant was a duly licensed life insurance agent authorized to sell just the type of policy involved in this case. (See Opinion of the trial court R. 46.)

The statement in the last paragraph on page 3 of appellant’s brief, and continuing over to page 4, concerning appellant’s insurance experience and training, was rejected by the trial court on the hereinabove referred to competent evidence.

It would be well to state at this point the legal truism that an appellate court is not concerned with conflicts in the evidence. It does serve to illustrate the weakness in appellant’s position that he finds it necessary to refer to his own testimony, which the trial court quite properly rejected. In our statement of facts, we have already referred to the policy loans mentioned on page 5 of appellant’s brief and have pointed out the testimony showing the separation of the cash and loan values from the special privilege provisions in the policy; no further comment is necessary upon this subject.

### THE QUESTIONS PRESENTED.

Although a number of questions were raised in the "Statement of Points" on page 6 of appellant's brief, only three of them are actually discussed in the argument, namely,

1. Is the present action barred by laches;
2. Was the insured prejudiced; and
3. Does the incontestable clause of the policy bar the present proceeding.

Appellant concedes, as he must, that there was sufficient evidence for the trial court to find, as it did find, that there was a mutual mistake in issuing the policy sufficient to entitle appellee to the relief prayed for in the Complaint. (Appellant's Brief, page 14.) For this reason, appellee will offer no argument on that subject in this brief. The other questions hereinabove set forth will be discussed hereafter.

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### ARGUMENT.

#### I.

#### APPELLEE'S ACTION WAS NOT BARRED BY LACHES NOR WAS THE ASSURED PREJUDICED.

Appellee deems it expedient to discuss these questions together.

##### A. Laches.

Appellee will hereafter have occasion to call this court's attention to a number of cases wherein the defense of laches was raised under factual situations



similar to those presented by the case at bar. However, since this point constitutes one of appellant's main grounds of appeal, some preliminary observations on the subject should not be amiss at this time.

The doctrine of laches is as old as equity itself. In California, there are numerous cases dealing with this subject and some general principles should be observed. The courts of California have said that laches is founded principally upon the equitable maxims "That he who seeks equity, must do equity"; "He who comes into equity, must come with clean hands"; "And the law serves the vigilant, and not those who sleep upon their rights". The propriety of the application of the rules depends upon the conduct and situations of all of the affected parties, not solely upon one.

*Smetherhan v. Laundry Workers Union*, 44 Cal. App. (2d) 131.

It is fundamental that laches is a defense and the burden of proving the facts from which it may be inferred rests upon the party who invokes the doctrine. In all cases *laches is a question of fact*, on the evidence, and each case becomes largely a law unto itself. In other words, the matter is one which reposes in the sound discretion of the chancellor.

*Brown v. Oxtoby*, 45 Cal. App. (2d) 702.

Finally it must be borne in mind that the doctrine of laches is to be invoked only where by reason of the plaintiff's acts the allowance of the claim would work an unwarranted injustice.

*Long v. Long*, 76 Cal. App. (2d) 716.



The bare recitation of the foregoing rules should be sufficient to dispose of appellant's claim as applied to the facts of this case. Turning to the insurance cases, we find a number of them in which reformation was decreed under circumstances at least as favorable to appellee and, in some of them, the circumstances were not as favorable to the person who was held entitled to reformation.

One of the leading cases on this subject is *Columbia National Life Insurance Co. v. Black*, 35 Fed. (2d) 571. The error in the policy in that case was discovered by the company *two months after the policy was issued*. Shortly thereafter, the company sold out to another company, which, although charged with the knowledge of its predecessor, did not in fact know of the error. At the end of twenty (20) years, when the option became available to the assured for the first time (the option being the portion of the policy where the mistake was made), he, the insured, demanded the amount which the mistake gave him. Immediately thereafter, suit was brought to reform the policy. The United States circuit court of appeal, for the tenth circuit, decreed reformation. The defense of laches was interposed and rejected despite the lapse of twenty (20) years in bringing the action. It will be observed that the defense stood on much sounder ground than it does in the case at bar for the reason that the error was discovered two (2) months after the issuance of the policy and no action was taken for twenty (20) years. This case will have to be observed again when we come to discuss the question of prejudice. For that

reason, it will not be referred to at this point any further. It is significant to note, however, that, in the case at bar, the action for reformation was brought within a matter of a very few months after the error was discovered and well within the time prescribed by the law of the State of California, which is that an action for relief on the ground of a mistake may be brought at any time within three (3) years from the accrual of the cause of action. The cause of action is not to be deemed to have accrued *until the discovery, by the aggrieved party, of the facts constituting the mistake. Code of Civil Procedure, Section 338, Subdivision 4.* (Italics ours.)

It should be pointed out to the court at this time that throughout his brief, appellant has completely overlooked the italicized portion of the law hereinabove referred to and this, notwithstanding the fact that the trial court, in its very able memorandum, stated as follows:

“Finally, laches is raised as a defense. Section 338 of the California Code of Civil Procedure has no bearing. The limitation there prescribed, by the expressed wording of the statute, does not begin until discovery of the mistake. Mere lapse of time may not constitute laches which will bar reformation, ‘particularly where the party seeking reformation has been ignorant of the defect which he seeks to have corrected’. 44 C.J.S. 1116.”

In *Prudential Insurance Co. of America v. Deane* (Delaware) 27 Atl. (2d) 365, the company did not discover the mistake in the policy for twenty (20) years,

during which time the assured paid all of the premiums. The court decreed that the company was entitled to have the policy reformed, notwithstanding the lapse of twenty (20) years. In so doing, the court used the language cited by the trial court in its memorandum decision below as follows:

“No prejudice to respondents from the delay of twenty years, nor ‘change of situation during neglectful repose’ have been demonstrated. Complainant is willing that the insured should have all for which he bargained and paid. In consequence, the defense of laches must fail.”

It is to be observed that the cited case is strikingly similar to the case at bar.

In *Buck v. Equitable Life Insurance Society* (Wash.), 165 Pac. 878; 96 Wash. 683, the action to rectify the mistake was held properly brought and reformation was decreed even at the end of fifteen (15) years.

In *Youngs v. Metropolitan Life Insurance Co.*, 28 Ohio NPNS 179, reformation was decreed despite the lapse of twenty (20) years.

In *Berry v. Continental Life Insurance Co.* (Mo.) 33 S.W. (2d) 1016; 224 Mo. App. 1207, reformation was granted after twenty (20) years.

In *New England Life Insurance Co. v. Jones*, 1 Fed. Supp. 984, where the error was not discovered until the assured's death six (6) years after the issuance of the policy, reformation was decreed.

In each and all of the foregoing cases, the company, through error of its scrivener or some employee of the company, had erroneously inserted something in the policy for which the assured did not apply or pay. In some of the cases cited, the assured loudly asserted that he knew of no mistake on his part. Had the appellant in this case raised the question on appeal that there was no mistake, it would have been necessary to analyze the mistakes made in the respective cases at some length and call to this court's attention the disposition made of those claims. However, the cases have been cited to this court on the sole proposition that the defense of laches was interposed and rejected in each of them. As has already been observed, the facts in some of the cases were much weaker on the question of laches than those in the case at bar.

It was uncontradicted that appellee had no actual knowledge of the mistake in the case at bar until the matter was called to its attention by the Crocker First National Bank of San Francisco in March of 1946. The action in the case at bar was filed on August 19, 1946, within six (6) months after the discovery of the error and after negotiations with the assured to have him submit the policy for voluntary reformation had failed. How it could be said that appellee was guilty of laches under such circumstances is inconceivable.

We turn now to the argument and authorities submitted on this subject by appellant. We observed in the first instance that the burden of establishing the defense of laches was upon appellant and that laches is a question of fact. Even if it be assumed that the



evidence would have supported a finding of laches, which we cannot in view of the record, still the trial court's finding on this subject could not be disturbed by an appellate court. Again the defense of laches, it must be remembered, is based upon the equitable principle that he who seeks equity must do equity. This principle works both ways. By his very resistance of this action for reformation, appellant refuses to do equity; he seeks instead to receive from appellee a sum in excess of \$10,000.00, for which he neither applied nor paid and he bases his right to recovery upon the fact that appellee, admittedly by mutual mistake, inserted such a provision in the policy of insurance actually issued to him.

The principal argument on this subject is based upon the fact that the policy was in the hands of appellee at the time of its issuance and also for loan purposes on four (4) separate occasions. The trial court found in the very finding cited by appellant (Finding 16, R. 55, et seq.) that, although the policy was in appellee's hands, it discovered no error in said policy while completing any loan thereon, and found specifically in said finding that appellee's first knowledge of the mistake was in March of 1946.

The tryer of the facts, the trial court in this instance, might have been impressed with an argument such as is made by appellant on this subject, namely, that because the policy was in the hands of one branch of the company which had nothing to do with its issuance, it should, nevertheless, have discovered the mistake, but that was an argument to be addressed to the tryer



of the facts in the trial court. The trial court in this case, quite properly we submit, found to the contrary, and adopted appellee's position that this was a separate branch of the company, that in making a loan on the policy it had no occasion to refer to the special privilege section thereof, and, therefore, it was not constructively chargeable with such knowledge. In any event, the argument is specious when addressed to an appellate court, which is unconcerned with either conflicting facts or conflicting inferences which may be drawn from admitted facts. There is nothing in the entire record to indicate, even as a question of fact, that appellee had any knowledge of the admittedly mutual mistake until March of 1946, after which it acted in the manner prescribed by both law and equity. It is submitted that the trial court quite properly held that the California statute of limitations did not begin to run until the discovery of the admittedly mutual mistake in March of 1946. Its findings in this respect are not only supported by the evidence, but are, indeed, the only reasonable findings which could have been made on the subject.

The authorities cited by appellant cannot assist him.

The first of these is *Yablon v. Metropolitan Life Insurance Co.*, (Ga.) 38 S. E. (2d) 534. Why appellant cited this case to this court on the subject of laches appellee cannot understand. On page 9 of his brief, appellant quotes the language of the Georgia Appellate Court to the effect that the question of laches in that case was one of fact and "did not justify the direction of a verdict that the company

had been so guilty''. The case went off on the proposition that the evidence did not show such a mistake as is relievable in equity, and further that the insured was so ignorant that he could not have been aware of the mistake if one was made. Since there is no question raised concerning the mistake in the case at bar on this appeal, it is difficult to see how the *Yablon* case is in point at all.

Although appellant, on page 14 of his brief, states, "Frankly, we do not think there was any mutual or other mistake in issuing the policy, *but refrain from arguing the point* only in view of the adverse findings of the trial court," it is difficult to know upon what proposition the language from 32 Corpus Juris 1142, etc. is quoted for (page 10, Appellant's Brief), except on that proposition. All of the cases cited by appellee on the question of laches held that there was a mistake such as entitled the insurance company to relief and such is the general law. (See Couch's Cyclopaedia of Insurance Law, Section 392.) Every mistake is in some sense the product of negligence, but equity has uniformly relieved from mistake in a proper case. Appellee does not contest the general propositions set forth by appellant on pages 10 and 11 of his brief, but simply submits they are inapplicable in view of the findings and authorities hereinabove cited.

Appellant seems to argue on page 11 of his brief that, because a person is chargeable with knowledge of the contents of a written contract signed by him, therefore, such a contract is not subject to reforma-

tion. This proposition is untenable and the authorities cited by appellant in support of it do not so hold. If this proposition were correct, no written contract would ever be subject to reformation. In each of the cases cited by appellee, a written contract of insurance was held subject to reformation. To state that a person has been negligent in issuing a contract in a particular manner makes him guilty of laches, is to beg the question.

The next cited case is *Metropolitan Life Insurance Company v. Asofsky*, 38 Fed. Supp. 464. In that case, the company claimed a mistake in the premium called for by the policy in that it was based upon age 60 and not age 65, the assured's age. Plaintiff conceded that the assured had no knowledge as to the amount of the premium, which was never discussed during the solicitation for the policy. The subject of laches is not even discussed in the opinion and the case goes off on the sole issue that the mistake was unilateral and there was no fraud or inequitable conduct on the part of the insured. That there has been bilateral mistake and fraud and inequitable conduct on the part of appellant is settled by the findings and the evidence in this case. It is true, as stated on page 12 of appellant's brief, that there was no fraud in connection with the original issue of the policy or with any of the policy loans. The situation in connection with the policy loans has already been completely disposed of heretofore and it would serve no useful purpose to reiterate in detail the complete separation of the loan and underwriting departments of appellee at this time.

The remaining argument, on page 12 of appellant's said brief, completely overlooks the issues in the case. Appellee can think of no better answer to give appellant than that which has already been given by the trial court as follows:

"I think the evidence required a finding of mutual mistake \* \* \* It is incredible that defendant (appellant) did not familiarize himself with the special privileges. He was not a novice in the business world. He admits that he read the policy, apparently shortly after he received it \* \* \* I am satisfied that he read these provisions and, if he did read them, he must have realized that a mistake had been made. He was an agent of plaintiff (appellee), authorized to write just such policies \* \* \* He was aware that his company could not issue generally the policy which was issued and remain in business. No other conclusion comports with the facts. \* \* \*

*"He knew that he applied for a different kind of policy than the one delivered. He must have known the benefits appurtenant to such a policy, both at the time he signed the application and at the time he received the policy. The discrepancies between the two are great. The policy revealed to him a patent error.*

"The conclusion reached is that defendant (appellant) *did notice the error but kept it to himself.*" (Italics ours. R. 45-47.)

The foregoing language of the trial court likewise is a complete answer to the argument made in the last paragraph of appellant's brief commencing on page 12.



The next cited case is *Dutton v. Prudential Insurance Co.*, (Mo.) 193 S. W. (2d) 938. Once again we are faced with the citation of a decision which does not even discuss the question of laches. The case is apparently cited for the proposition stated on page 12 of appellant's brief that there must be certainty of error before reformation will be granted. That there is such certainty in the case at bar can hardly be disputed. In the cited case, there was no evidence of any mistake whatsoever and it was quite properly held that no reformation would be granted.

On page 13, appellant states that there was no evidence that the wrong printed form of policy was selected in the case at bar. It is submitted that, in the statement of facts, appellee has set forth the evidence from which the trial court could draw no other inference whatsoever and apparently appellant concedes the point on page 14 of his brief and seeks instead to avoid the result of such a mistake by pleading laches. We have already commented on the *Dutton* and *Yablon* cases cited at this point. The case of *Hayes v. The Travelers Insurance Company*, 93 Fed. (2d) 568, is also cited. This was another case where there was a finding of no mistake; the case does not turn on the question of laches at all.

Finally, appellant cites the case of *Kaufman v. New York Life Insurance Co.*, (Penn.) 172 Atl. 306. This is another case where the question of laches was not even discussed. Although the court refused reformation, the case is in reality an authority in support of appellee's position. It reviews the decisions which we



have heretofore cited on the question of laches, not on that question, but on the question of mistake for which proposition appellant apparently is citing the case. For example, referring to *Columbia National Life Insurance Co. v. Black*, supra, a case relied upon by appellee herein, the court said:

“As the court clearly pointed out, there was a patent and manifest absurdity on the face of the policy, a reformation was consequently allowed to rectify the error.”

The reason the court refused reformation in the *Kaufman* case was because the discrepancy was so small; the mistake in that case made a difference of but \$420.00. In the case at bar, it makes a difference in excess of \$10,000.00. The smallness of the mistake in the *Kaufman* case was the sole reason the court refused to grant reformation. The court, in the *Kaufman* case, admits that, where the mistake is so great that the assured must have recognized the error, reformation will be decreed upon the ground that a mistake by one party, coupled with knowledge thereof by the other, affords a basis of equitable relief. The court said:

“It has been held with obvious justice that a mistake by one party and knowledge of the mistake by the other, will justify the relief as fully as mutual mistake.”

On page 15, appellant claims that he is ignorant. The language of the trial court heretofore quoted will serve to illustrate the futility of this position.

Although, as we have already observed, appellant apparently abandoned in this court his claim that there was no mistake cognizable by a court of equity, he has seemingly blown hot and cold on this subject. In one breath he says he refrains from arguing the point in view of the adverse findings of the trial court; in the next, he cites cases involving mistake and loudly proclaims innocence. For that reason we carefully invite the court's attention to the cases which we have heretofore cited on the proposition that there was no laches involved in the case at bar. In each of them, the court will find that there was a mistake, sometimes infinitely smaller than that presented here and we feel it particularly appropos to quote the language of the United States Circuit Court of Appeal, for the Tenth Circuit, in the case of *Columbia National Life Insurance Co. v. Black*, supra, as follows:

“While courts are properly reluctant to alter the terms of a written engagement, even in equity, and do not do so unless the proof is clear and convincing, we are of the opinion that the uncontradicted and indisputable facts in this case require the interposition of equity. It is true the defendant on the stand and in his letters denies any mistake on his part. But his actions speak louder than his words. He applied for an ordinary life policy; without any quibble, and in response to his application, he received a policy that manifestly was in error. He only paid for an ordinary life policy. When he received the policy he either did or did not notice the error. If he did not notice it, the mistake was mutual. If he did notice it and said nothing, he was guilty of

such inequitable conduct as to amount to fraud. A man presents a check for \$100 to a bank teller; he gets two \$100 bills. No matter how loudly he asserts the lack of mistake on his part, the fact still remains that he was either mistaken or was trying to benefit by the teller's mistake. Without resorting to any oral evidence, the papers in this case on their face bear conclusive proof of a mistake that can be and should be corrected in equity."

Throughout his entire brief, but principally in connection with his discussion on the question of laches, appellant has made frequent reference to appellee's negligence. For that reason, we deem it appropriate to quote the following language from *Columbia National Life Insurance Co. v. Black*, supra:

"It is claimed that the company was negligent in failing to discover the error, and attention is called to a statment on the policy reading: 'Examined by J. M. S.' Apart from the question whether negligence must be accompanied by prejudice, it is sufficient to say that negligence is not in itself a defense, else there would be no ground for reformation for mistake, as mistakes nearly always presuppose negligence."

**B. There was no prejudice to the insured.**

In a very brief paragraph on page 16, the appellant claims that he was prejudiced. This argument is fully answered by the case of *Columbia National Life Insurance Co. v. Black*, supra, as follows:

"It is true that the plaintiff in error, or its predecessor, knew of this error for 20 years, and

brought no action to rectify it. It does not appear that the defendant was prejudiced by this delay. The defendant testified that, because he held this policy, he let others lapse; but he cannot seriously contend he lapsed these other policies on the hope of some day getting more than he asked for or paid for from this policy; and if he did, and is disappointed, the prejudice results not from the delay but from his illbegotten hope."

Appellee submits that the prejudice argument is clearly specious.

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## II.

### THE PRESENT ACTION IS NOT BARRED BY ANY STATUTE OF THE STATE OF CALIFORNIA.

It has already been pointed out that Section 338 of the California Code of Civil Procedure gives a period of three years from the *time of the discovery* by the aggrieved party of the facts constituting the fraud or mistake within which a person may legally bring an action for relief. The present action was brought well within that time.

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## III.

### THE INCONTESTIBLE CLAUSE DOES NOT BAR THE PRESENT ACTION.

The futility of appellant's position is well illustrated by the argument made on this subject. Originally, in the trial court, he abandoned this defense. The incontestable clause of a policy means exactly



what it says, that is, no action which has for its purpose the contesting of the policy may be brought after the time for a contest elapses. But an action for reformation is not an action to contest the policy, it is an action to affirm the policy and to correct a mistake in it. There is no question of avoidance of the policy. The policy is not being contested and this is the feature which distinguishes the case at bar from the cases cited in appellant's brief.

Appellant in his brief has not cited a single case to this court holding that an action for reformation constitutes a contest of the policy within the meaning of the incontestable clause. These cases will be noted shortly.

The point has been directly passed upon that an action to reform a policy *is not* a contest within the meaning of said clause. In *Columbia National Life Insurance Co. v. Black*, 35 Fed. (2d) 571, 577, the policy applied for and the one issued each contained an incontestable clause similar to that which is now before the court. The only express saving portion of the clause was non-payment of premiums exactly as in the case at bar. The court held that the reformation action was not an action to contest the policy within the meaning of the clause and, in so doing, stated as follows:

“Both the policy applied for and the one issued provide, in substance, that ‘after one year from date hereof this policy shall become incontestable,’ save for nonpayment of premiums. It is claimed that this provision bars this action. The conten-



tion is not sound. *This is not a contest of the policy but a prayer to make a written instrument speak the real agreement of the parties.* It would hardly be suggested that an assured, who brings an action to reform a policy and to recover under it as reformed, was contesting the policy within the meaning of this clause. Yet the clause is not one-sided, and the right of the assured to have the writing express the agreement actually made is no greater than the right of the assurer. We have found no authority upon the point, although there are many decided cases involving the construction and scope of the clause. Reference is made to *Mack v. Connecticut General Life Ins. Co. of Hartford*, 12 F. (2d) 416 (8 C.C.A.); *Myers v. Liberty Life Ins. Co.*, 124 Kan. 191, 257 P. 933, 55 A.L.R. 542; *Scales v. Jefferson Standard Life Ins. Co.*, 155 Tenn. 412, 295 S.W. 58, 55 A.L.R. 537, and the Annotation in 55 A.L.R. 549, for general discussions of the clause. Without going at length into the purpose and history of the clause and without intimating that an actual contest may not be found under the cloak of reformation, *we hold that an action to correct a purely clerical error in a policy issued, so that it will speak the truth as to the agreement of the parties, is not barred by the incontestable clause.*" (Italics ours.)

In *Mates v. Penna. Mutual Life Insurance Co.*, (Mass.) 55 N.E. (2d) 770, decided by the court as late as June 1, 1944, the same defense was urged under a similar incontestable clause and a number of cases were cited. The following language would seem to be most persuasive:

“The plaintiff contends that that provision makes it now too late for the defendant to show the mistake. In our opinion, the correction of the policy to express the true agreement is not contesting the policy within the meaning of that provision. See *Columbia National Life Ins. Co. v. Black*, 10 Cir., 35 F. (2d) 571, 71 A.L.R. 128; *Equitable Life Assurance Society v. Rothstein*, 122 N. J. Eq. 606, 195 A. 723, affirmed 123 N. J. Eq. 591, 199 A. 43; *Neary v. General American Life Ins. Co.* 140 Neb. 756, 1 N.W. (2d) 908. See also *Reagan v. Union Mutual Life Ins. Co.*, 189 Mass. 555, 76 N. E. 217, 2 L. R.A., N. S., 821, 109 Am. St. Rep. 659, 4 Ann. Cas. 362.”

Appellee has no quarrel with the cases cited by appellant on this subject. They are all cases involving an attempt by the company to avoid payment on the policy at all, as distinguished from cases which attempt to make the policy speak the true agreement of the parties. The principal case relied upon by appellant on this subject is *Dibble v. Reliance Life Insurance Co.*, 170 Cal. 199. This was an action to *cancel the policy* for false representations and statements. The policy was, in fact, being contested. In the case at bar there is no deception; the company seeks to give the assured exactly what he applied for and what he paid for; nothing more, nothing less. The language heretofore cited from the *Black* and *Mates* cases, *supra*, constitute a complete answer to the argument made on pages 21-24 of appellant's brief.

## IV.

**THE TRIAL COURT'S OPINION.**

The trial court's opinion is attacked. The learned trial judge gave to this case the most careful consideration and rendered an opinion herein which shows a complete knowledge and understanding of the facts and the law applicable thereto. That opinion is contained in the record which is before this court and needs no defense from appellee herein. We must observe, however, that the attack made upon it is wholly unwarranted.

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**CONCLUSION.**

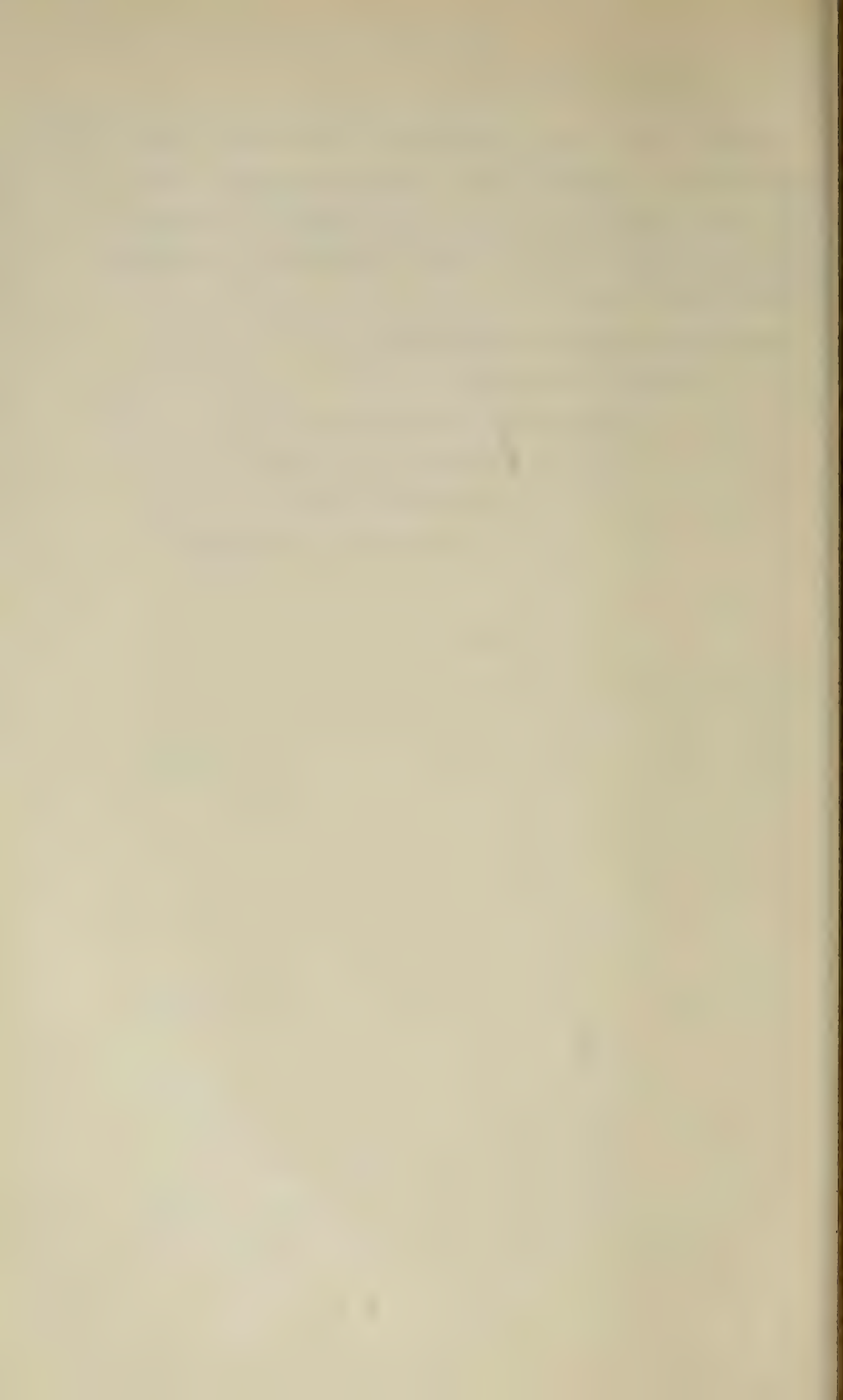
In conclusion, it is submitted that appellant has cited no authority to this court which would even remotely justify it in disturbing the trial court's judgment. The facts clearly show, as found by the trial court, both a mutual mistake, as evidenced by the application for the policy of insurance and also upon such a patent and obvious mistake, that it would be a fraud upon the part of the appellant to insist upon the performance of the policy according to its written, but unapplied for and unpaid for, terms. The record shows quite conclusively that appellee acted seasonably to assert its rights. To permit appellant to prevail in this case would amount to his enrichment in a sum exceeding \$10,000.00, for which he neither applied nor paid. The trial court quite properly held that he would not be allowed this unjust profit.

Finally, equity has consistently ruled that he who seeks equity must do equity. Is it doing equity to insist upon receiving more than \$10,000.00 without paying for it? The trial court's judgment should be affirmed in its entirety.

Dated, San Francisco, California,  
October 25, 1948.

Respectfully submitted,  
JOSEPH T. O'CONNOR,  
HAROLD H. COHN,  
*Attorneys for Appellee.*





No. 11,917

IN THE  
United States  
Court of Appeals  
For the Ninth Circuit

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GEORGE H. RICHARDSON,

*Appellant,*

vs.

THE TRAVELERS INSURANCE COMPANY,

*Appellee.*

---

APPELLANT'S ANSWERING BRIEF

---

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## Subject Index

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	Page
Answering Appellee's Contentions.....	3
The Incontestable Clause.....	4
The California Statute of Limitation Applies.....	5

## Table of Authorities Cited

---

	Pages
CASES	
Bathke v. Rahn, 46 Cal. App. (2d) 694, 696.....	6
Dibble v. Reliance Life Ins. Co., 170 Cal. 199.....	3, 4
Green, Malone Motor Co. v., 215 Ala. 635, 105 So. 897, 898...	6, 7
Lady Washington Con. Co. v. Wood, 113 Cal. 482, 487.....	6
Malone Motor Co. v. Green, 213 Ala. 635, 105 So. 897, 898...	6, 7
Rahn, Bathke v., 46 Cal. App. (2d) 694, 696.....	6
Reliance Life Ins. Co., Dibble v., 170 Cal. 199.....	3, 4
Siem, In Re, 284 Fed. 868, 872.....	5
Wood, Lady Washington Con. Co. v., 113 Cal. 482, 487.....	6
STATUTES	
California Code of Civil Procedure Sec. 338.....	3, 5, 6, 7



No. 11,917

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**United States  
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For the Ninth Circuit

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GEORGE H. RICHARDSON,

*Appellant,*

vs.

THE TRAVELERS INSURANCE COMPANY,

*Appellee.*

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**APPELLANT'S ANSWERING BRIEF**

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We are not unmindful of the settled rule that where the trier of fact makes findings upon conflicting evidence, no question, on that issue, is presented to an appellate court. However the large number of reversals, on appeal of lower court judgments, attests convincingly to the non-infallibility of trial court findings.

Where, as here, a case is tried and findings made, adverse to the appellant, who feels, in his own mind nevertheless, that an injustice has been done to him, and the trial court has "found" facts which he believes are incorrect, his only recourse, in view of the rule just stated, is to urge what technical objections exist, in order to obtain the simple justice which he feels is his due. Appellant sincerely claims that his testimony as given in the lower court (particularly R. 119) was true, correct and pertinent in all respects—that there was no mistake in the issuance of the policy as originally written, and that the policy as issued, was in exact accordance with the previous conversations and understanding he had with Mr. Glendenin and Mr. Hensley, appellee's then (1926) assistant managers (R. 120) and that the policy is the same one he discussed, thought he applied and paid premiums for, and that the lower court's judgment gives him only one-half the amount he believes he paid for and should now receive.

Appellee is incorrect in assuming that appellant refrained from arguing the findings because he accepted these findings as true and conclusive of the actual facts. We refrained from arguing them in our opening brief, and limiting our argument before this court to the technical questions involved, solely because of the rule stated above.

We think most of the argument contained in appellee's brief, is already answered by our opening brief, and we shall refrain from belaboring the Court with further and repetitious argument along similar lines. However, we do wish to make a few observations of so-called "new matter" (not previously stressed) contained in appellee's brief.

### ANSWERING APPELLEE'S CONTENTIONS

It would appear to us that appellee's argument regarding the general subject of laches and statutes of limitations and repose, could better be addressed to the Legislature, as an argument against any type of statute of limitations.

In speaking of such statutes, the late Chief Justice Angelotti, of the California Supreme Court, in *Dibble v. Reliance Life Ins. Co.*, 170 Cal. 199, quoting from *Wright v. Mutual Benefit Assn.*, 118 N.Y. 237, 16 Am. St. Rep. 749, 6 L.R.A. 731, 23 N.E. 186 said (of our California C.C.P. Sec. 338):

“It is in the nature of and serves a similar purpose as statutes of limitations and repose, *the wisdom of which is apparent to all reasonable minds.*” (Italics ours)

It is axiomatic and elementary that the findings of a trier of fact, are no better than the evidence upon which they are based, and that findings made contrary to the admitted and obvious facts, cannot stand; e.g., suppose, for instance, that a trial court was to make findings that a certain well known Japanese was a white person of the Caucasian race but when the case was heard on appeal, the person concerned was personally present in the appellate court, and a casual glance would at once establish the inaccuracy of the lower court's findings. Findings made under such circumstances, no matter in what legal or judicial verbiage cached, cannot possibly stand. The cases in this court on this elementary point are legion. Appellant feels the present findings come within this category.

The Supreme Court of Pennsylvania in *Kaufman v. New York Life Ins. Co.*, 315 Pa. 34, 172 Atl. 306, beginning at page 307, distinguishes *Columbia Natl. Life Ins. Co. v. Black*, 35 Fed.(2d) 571 (C.C.A. 10th) and most of the other cases cited by appellee in his brief, from cases similar to the case at bar, in our opinion. Besides, in none of the cases cited by appellee, including *Columbia Natl. Life Ins. Co. v. Black*, supra, were the policies delivered into the hands of the insurer company in connection with policy loans. This fact alone, we submit, is enough to distinguish *Columbia Natl. Life Ins. Co. v. Black*, supra, from the instant case.

### THE INCONTESTABLE CLAUSE

Appellee's statement on page 22 of his brief, that we originally, in the trial court, abandoned our defense of the incontestable clause, is grossly inaccurate. The whole record of the proceedings in the court below is now before this court, and nowhere does this appear. We positively did not abandon that defense then, and we do not abandon it now.

Appellee says he has no quarrel with the cases cited by us, particularly, *Dibble v. Reliance Life Ins. Co.*, supra. The law is too well settled to now admit of a quarrel. But it is significant to observe that largely the same arguments then being made against the incontestable clause regarding procuring the policy by fraud, are now being advanced by appellee herein against the incontestable clause in this suit for reformation.

We again respectfully submit that it cannot be held that the incontestable clause in the present policy does not



apply in this present "reformation" suit, without outraging and doing violence to the plain and unequivocal language of the incontestable clause in the policy; and we submit that no amount of legal verbiage could ever convince the "man in the street"—the average policyholder—who buys life insurance—that a suit by the company to "reform" the policy 20 years later, and pay only one-half the amount clearly stated in the policy, is not a "contest" of the policy which he supposed he was protected against by the incontestable clause in his policy.

Appellee complains in his brief (page 13) and says that appellant is guilty of "inequitable conduct" because he had the temerity to resist and defend appellee's present action to reform the insurance contract 20 years after its issuance—and pay appellant only one-half the amount clearly stated in his policy.

To this outrageous and un-American claim we can only refer to the language of Judge Bourquin in *In re Siem*, 284 Fed. 868, 872, where in speaking of an absurd defense the court said:

"\* \* \* savors much of the tyrant's bitter complaint that his victims refused to die quietly, and disturbed his sleep with their indecent wails of agony."

### **THE CALIFORNIA STATUTE APPLIES**

Without regard to the other reasons assigned in our opening brief as to why this case should be reversed—all of which points we still feel are good, and urge—we think one point above all is unanswerable, namely:

Appellee on page 10 of his brief, appears to recognize the applicability of the California statute of limitations (C.C.P. Sec. 338, Subd. 4) and claims in avoidance, that



“\* \* \* appellant has completely overlooked the italicized portion of the law hereinabove referred to \* \* \*”. The italicized portion of the statute referred to reads “*The cause of action is not to be deemed to have accrued until the discovery, by the aggrieved party, of the facts constituting the mistake.*” (Italics ours)

This phase of the case is now clear, and in view of the settled law on the subject, we submit, requires a reversal on this point alone, for the following reasons:

*First:* It is the settled law in California, and elsewhere, that “Means of knowledge, is the equivalent of knowledge.” In *Lady Washington Con. Co. v. Wood*, 113 Cal. 482, the California Supreme Court at page 487, said:

“\* \* \* as the means of knowledge are equivalent to knowledge, if it appears that the plaintiff had notice or information of circumstances which would put him on inquiry which, if followed would lead to knowledge, or that the facts were presumptively within his knowledge, he will be deemed to have had actual knowledge of the facts. These principles are so fully recognized that mere reference to some of the cases in which they have been enforced will be sufficient. (Martin v. Smith, 1 Dill. 85; Wood v. Carpenter, 101 U.S. 135; Hecht v. Slaney, 72 Cal. 363; Moore v. Boyd, 74 Cal. 167; Lataillade v. Orena, 91 Cal. 565; 25 Am. St. Rep. 219)”.

This rule has been consistently followed since. See *Bathke v. Rahn*, 46 Cal. App.(2d) 694-696. It is also followed in other jurisdictions. In *Malone Motor Co. v. Green*, 213 Ala. 635, 105 So. 897, the Supreme Court of Alabama at page 898 said:

“The means of knowledge is the equivalent of knowledge, and whatever is sufficient to put one on inquiry is sufficient to charge him with notice of everything to which the inquiry would lead.”

*Second:* We think it requires little argument to show that on each of the four occasions when the appellee had the policy back at its home office in Hartford, Conn., for a month at a time, in connection with the policy loans, it then had the “*means of knowledge*” and information, sufficient to put it upon inquiry and which if followed (such as merely reading the upper half of the same page on which appellee admittedly read the policy loan values) would certainly have led to the “discovery” of the now lately claimed error—but which in any event, is sufficient to charge it with notice of the exact terms of the policy—which terms remained in the policy at all times since its issuance in 1926 down to the present time.

*Third:* The appellee then, having had legal knowledge of the exact terms of the policy, as early as 1928 (first loan) and as late as 1936 (last loan) and not having seen fit to take action to commence the present suit until August, 1946, over 10 years later, now brings the present action squarely within the California statute of limitations (C.C.P. Sec. 338), including the “*italicized portions*” thereof.

*Fourth:* Appellee’s argument that its loan department had no “connection” with its policy writing department, or its other departments, we submit, is so ridiculous, absurd and downright silly, as to fall by its own weight. Indeed, perchance, if such a dangerous doctrine were to become the law, there would soon be no sanctity of con-

tracts and little responsibility under any sort of contract which would soon lead to open repudiation of most contracts including insurance policies. If such were the law, all an insurer would have to do to repudiate its policy would be to claim that its policy writing department had nothing to do with its sales department. Absurd? Surely; but no more absurd than appellee's present contention and "explanation" of why it didn't read the policy on any one of the four occasions it had the policy, not only in its home office in Hartford, Conn., but also when the policy passed through its San Francisco branch office.

It is again respectfully submitted that, for the reasons assigned, this case should be reversed and judgment entered for appellant for the full amount clearly and unequivocally stated in his policy.

Respectfully submitted,

ALVIN GERLACK,

Russ Building,  
San Francisco, 4,

*Attorney for Appellant.*

Dated: San Francisco, Calif.,

Nov. 5, 1948.

No. 11,917

IN THE

United States Court of Appeals  
For the Ninth Circuit

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GEORGE H. RICHARDSON,

*Appellant,*

vs.

THE TRAVELERS INSURANCE COMPANY,

*Appellee.*

APPELLEE'S PETITION FOR A REHEARING.

(Or, If a Rehearing Be Denied, For a Stay of Mandate.)

---

JOSEPH T. O'CONNOR,

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1948





## Table of Authorities Cited

---

	Page
Buck v. Equitable Life Assurance Society, 165 Pac. 878....	5
Columbia National Life Insurance Co. v. Black, 35 F. (2d) 571 .....	4
Dibble v. Reliance Life Insurance Co., 170 Cal. 199.....	2
Hunt v. Rhodes, et al., 1 Pet. (U.S.) 1, 7 Law. Ed. 1.....	3
Mates v. Pennsylvania etc. Co., 55 N. E. (2d) 770.....	5



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**APPELLEE'S PETITION FOR A REHEARING.**

**(Or, If a Rehearing Be Denied, For a Stay of Mandate.)**

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*To the Honorable Justices of the United States Court  
of Appeals for the Ninth Circuit:*

Appellee respectfully petitions for a rehearing of the above cause decided on December 13, 1948, and in support thereof urges that the decision of this Court, that the incontestable clause of the policy of insurance bars an action for reformation of the policy after the expiration of the time limit therein contained, is erroneous.

The opinion uses language that is not applicable to the facts of the case. The opinion states:

"It [this contract] is not a reference to the oral conversations and negotiations preliminary to the

execution of the written instrument, but rather to the formal writing itself.”

The mistake in this instance is not shown by oral conversations. It is shown on the written instrument itself. The application, made a part of the policy, designates one form of policy. Another part of the instrument designates a different form. The oral conversations introduced on behalf of the insurance company were merely to rebut a claim by the insured that he had been misled by statements alleged to have been made by employees of the company.

This Court, in its decision, relies almost exclusively on the cases which hold that the defense of fraud is barred by the incontestable clause contained in an insurance policy and reasons by analogy from such decisions.

See, for example:

*Dibble v. Reliance Life Insurance Co.*, 170 Cal. 199.

Appellee respectfully submits that an action for reformation on the grounds of mistake is not comparable to the defense of fraud in any way. It must be remembered that in this case the trial court found upon ample evidence, and this Court has apparently approved such finding, *that the only contract* entered into between appellant and appellee was that applied for in the application for insurance made part of the policy. (Plaintiff's Exhibit "A", R. 5.) If this be true, the only contract upon which there was a meeting of the minds and to which the incontestable clause in

the policy could apply was the so-called annuity form policy. If appellee sought to introduce any defense to *that* policy, the incontestable clause would apply. Such would be the defense of fraud. The defense of fraud seeks to avoid the policy and is, in fact, a contest of it. The policy to which this Court has held the incontestable clause applies is one that was never discussed by the parties and one which the trial court held, on the same competent evidence, never came into being. The action in the present case was not a contest of any contract of insurance. It was a proceeding in which appellee sought to have the true agreement of the parties expressed rather than a mistaken one. To hold that this is a contest of the policy begs the question.

We submit the opinion gives an erroneous interpretation of the words "This Contract". A written instrument is not itself the contract. It is evidence of the contract. A court of equity cannot make a contract. It may reform a written instrument to properly express the agreement entered into (see *Hunt v. Rhodes, et al.*, 1 Pet. (U.S.) 1, 7 Law. Ed. 1) and in this proceeding the change sought is not in the contract but in the evidence of the contract. The provision does not read "This written instrument shall be incontestable" nor "This policy shall be incontestable". By the term "This contract" reference is made to the contract of which the policy is but evidence.

Appellee is well aware of the history of the incontestable clause and the reasons why it was introduced into insurance policies. It is submitted, however, that



it is one thing to hold that an insurer should not be allowed to contest an otherwise valid contract upon which there has been a meeting of the minds and quite another to say that an insurer should not be permitted to protest that a contract, as written, does not express the actual meeting of the minds.

Although the incontestable clause in the policy is almost universally invoked by the insured and is primarily for his benefit, it is not limited by its terms to the insured and conceivably could be invoked by the insurer in a proper case. If the converse of the present case had occurred and the company by mistake had inserted a provision in the contract giving to the insured one-half the benefits that he applied and paid for, would any court hold that an action to reform such contract was barred by the incontestable clause? We believe, under such circumstances, a court would have no difficulty in saying to the insurance company that refused to live up to the agreement it made, but which is erroneously failed to express, "the only contract you entered into was the one upon which you had a meeting of the minds. You cannot take the insured's money and give him half of what he paid for, notwithstanding the incontestable clause". This rule should work both ways.

The only adjudicated decisions on this subject prior to the case at bar are the cases cited in this Court's opinion, to-wit:

*Columbia National Life Insurance Co. v. Black*,  
35 F. (2d) 571;

*Buck v. Equitable Life Assurance Society*, 165  
Pac. 878;

*Mates v. Pennsylvania etc. Co.*, 55 N. E. (2d)  
770.

These cases are uniform that the incontestable clause does not bar a suit for reformation. This Court, for the reasons stated in its opinion, has seen fit to reject these cases, but it is submitted that the reasons given by this Court are based upon the false assumption that a suit for reformation is a contest rather than an action to have the policy speak the true agreement of the parties and it is submitted that the only agreement to which the incontestable clause applies is the agreement upon which there has been a meeting of the minds and no other.

For the foregoing reasons a rehearing should be granted.

In the event of a denial of this petition, appellee intends to apply to the Supreme Court of the United States for a writ of certiorari and therefore prays for a stay of mandate of this Court for thirty (30) days in order to enable appellee to make such application.

Dated, San Francisco, California,  
January 7, 1949.

Respectfully submitted,

JOSEPH T. O'CONNOR,

HAROLD H. COHN,

*Attorneys for Appellee  
and Petitioner.*



CERTIFICATE OF COUNSEL.

We hereby certify that we are counsel for appellee and petitioner in the above-entitled cause and that in our judgment the foregoing petition for a rehearing is well founded in point of law as well as in fact, and that said petition for a rehearing is not interposed for delay.

Dated, San Francisco, California,  
January 7, 1949.

JOSEPH T. O'CONNOR,  
HAROLD H. COHN,  
*Counsel for Appellee  
and Petitioner.*





No. \_\_\_\_\_

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**United States**  
**Circuit Court of Appeals**  
**For the Ninth Circuit**

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HELMET P. LOYNING and JOHN ZWEIMER,  
*Respondents and Appellants,*  
vs.

B. P. LOYNING,  
*Petitioner and Appellee.*

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**APPELLEE'S BRIEF**

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RALPH J. ANDERSON  
*Attorney for Appellee  
and Petitioner*

THURBER'S  HELENA

FILED  
JUN 28 1948

PAUL P. O'BRIEN,  
CLERK



# INDEX

i

## SUBJECT INDEX

	Page
STATEMENT OF THE CASE .....	1
QUESTIONS INVOLVED .....	6
SUMMARY OF ARGUMENT .....	6
ARGUMENT .....	7
The State Court Decree of 1944 Is Void for Want of Jurisdiction and Is No Defense to This Pro- ceeding .....	7
Appellants Failed to Show a Change of Conditions Justifying Their Violation of the Federal Court Decree .....	23
Appellee Proved the Charge of Contempt .....	25
CONCLUSION .....	27

## TABLE OF CASES AND AUTHORITIES

12 Am. Jur., Contempt, Section 24, p. 406 .....	26
19 Am. Jur., Equity, Section 423, p. 290 .....	10
19 Am. Jur., Equity, Section 425, p. 292 .....	10
19 Am. Jur., Equity, Section 428, p. 294 .....	10
Bijou Irr. Co. v. Lower Latham Ditch Co., 67 Colo. 356, 184 Pac. 292 .....	17
Black Panther Oil & Gas Co. v. Swift, 69 Okl. 33, 170 Pac. 238 .....	13
Consolidated H. S. Ditch & R. Co. v. New Loveland & G. Irr. & L. Co., 27 Colo. 521, 62 Pac. 364.....	14
15 C. J., Courts, Section 652, p. 1176 .....	9
34 C. J., Judgments, Section 635, p. 404 .....	9
34 C. J., Judgments, Section 1641, p. 1159 .....	8
17 C. J. S., Contempt, Section 84, p. 111 .....	23
21 C. J. S., Courts, Section 492, p. 745 .....	14

	Page
21 C. J. S., Courts, Section 529, p. 808 .....	14
21 C. J. S., Courts, Section 539, p. 832 .....	9
30 C. J. S., Equity, Section 635, p. 1049 .....	10
30 C. J. S., Equity, Section 637, p. 1054 .....	10
30 C. J. S., Equity, Section 643, p. 1069 .....	10
43 C. J. S., Injunctions, Section 218, p. 956 .....	12
Cooper v. Brazelton, C. C. A. 5 Cir., 135 Fed. 476.....	8
Crippen v. Glasgow, 38 Colo. 104, 87 Pac. 1073 .....	24
De La Mater v. Graves, 69 Colo. 255, 193 Pac. 552.....	21, 23
El Paso & R. I. Ry. Co. v. Dist. Ct., 36 N. Mex. 94, 8 Pac. (2d) 1064 .....	17
Farmers Ditch Co. v. Boyd Lake R. & I. Co., 66 Colo. 29, 178 Pac. 561 .....	17
Fidler v. Gilchrist, 60 Ind. A. 363, 109 N. E. 796.....	9
Gulf M. & N. R. Co. v. Hill Mfg. Co., 127 Miss. 644, 90 So. 358 .....	9
Hazard v. Joseph W. Bowles Reservoir Co., 87 Colo. 364, 287 Pac. 854 .....	17
In re Philadelphia Rapid Transit Co., C. C. A. 3 Cir., 117 Fed. (2d) 730 .....	8
In re Rochester Sanitarium & Baths Co., C. C. A., 2 Cir., 222 Fed. 22 .....	9
Ironstone Ditch Co. v. Ashenfelter, 57 Colo. 31, 140 Pac. 177 .....	24
Jacob v. Lorenz, 98 Cal. 332, 33 Pac. 119 .....	24
Kline v. Burke Construction Co., 260 U. S. 226, 67 L. Ed. 226, 43 S. Ct. 79 .....	13
Kurtz v. Phila. & R. R. Co., 187 Pa. 59, 40 A. 988.....	9
Louden Irrigating Canal Co. v. Handy Ditch Co., 22 Colo. 102, 43 Pac. 535 .....	18

# INDEX

iii

Page

Mannix & Wilson v. Thrasher, 95 Mont. 267, 26 Pac. (2d) 373 .....	19
National Labor Relations Board v. Fed. Bearings Co., C. C. A., 2 Cir., 109 Fed. (2d) 945 .....	23
Nelson v. Bailey, 303 Mass. 522, 22 N. E. (2d) 116...	11
People v. Sterling, 357 Ill. 354, 192 N. E. 229 .....	11
Princess Lida v. Thompson, 305 U. S. 456, 83 L. Ed. 285, 59 S. Ct. 275 .....	13
Rickey Land & C. Co. v. Miller & Lux, 218 U. S. 258 54 L. Ed. 1032, 31 S. Ct. 11 .....	13
Sain v. Montana Power Co., D. C., Mont., 5 F. Supp. 792 .....	18
Sain v. Montana Power Co., C. C. A., 9 Cir., 84 Fed. (2d) 126 .....	18
Sain v. Montana Power Co., D. C., Mont., 20 F. Supp. 843 .....	11, 20, 27
Spring Creek Irr. Co. v. Zollinger, 58 Utah 90, 197 Pac. 737 .....	25
State ex rel. Boston & Montana, etc., Min. Co. v. Clancy, 30 Mont. 193, 76 Pac. 10 .....	19
State ex rel. Reeder v. Dist. Ct., 100 Mont. 376, 47 Pac. (2d) 653 .....	11
State ex rel. Swanson v. Dist. Ct., 107 Mont. 203, 82 Pac. (2d) 779 .....	20
Thrasher v. Mannix & Wilson, 95 Mont. 273, 26 Pac. (2d) 370 .....	19, 24
Weiland v. Reorganized Catlin Consol. Canal Co., 61 Colo. 125, 156 Pac. 596 .....	15, 21
Wayne v. McBirney, 195 Okl. 269, 157 Pac. (2d) 161 .....	9
Whitcomb v. Murphy, 94 Mont. 562, 23 Pac. (2d) 980	11





**United States**  
**Circuit Court of Appeals**  
**For the Ninth Circuit**

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HELMET P. LOYNING and JOHN ZWEIMER,  
*Respondents and Appellants,*  
*vs.*  
B. P. LOYNING,  
*Petitioner and Appellee.*

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**APPELLEE'S BRIEF**

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**STATEMENT OF THE CASE**

The history of the litigation leading up to this contempt proceeding is somewhat involved, and it is therefore believed desirable, for a clearer understanding of the issues in this case, to discuss the evidence in greater detail than is set forth in appellants' brief.

In this proceeding the appellants, Helmet P. Loyning and John Zweimer, are charged by the appellee, B. P. Loyning, with contempt of court for violating the decree of the Circuit Court of the United States, Ninth Judicial Circuit, District of Montana, in cause No. 666, which decree was entered on the 28th day of May, 1906 (Tr. 88-91). That was a suit brought by W. A. Morris against several defendants, including W. R. Bainbridge and C. H. Young, predecessors in interest of Helmet P. Loyning

and John Zweimer, respectively, to enjoin the defendants from interfering with the flow of water in Sage Creek and its tributaries. T. N. Howell, predecessor in interest of B. P. Loyning, filed a complaint in intervention in said action (Tr. 50-59) claiming a water right subsequent to that of the plaintiff but prior to that of each of the defendants. At that time Howell was appropriating water from Sage Creek at a point in the state of Wyoming and the defendants were appropriating water from Piney Creek in Montana. In the pleadings filed in that action it was admitted that Piney Creek was a tributary of Sage Creek (Tr. 63, 64, 65-66, 68, 70, 71, 101). The decree in that action awarded Howell, predecessor in interest of B. P. Loyning, "one hundred and ten inches of the waters of Sage Creek and its tributaries . . . prior in time to any and all of the defendants" and perpetually enjoined the defendants and their successors in interest "from in any manner interfering" with said right (Tr. 89). There was no specific finding by the court that Piney Creek was a tributary of Sage Creek since this was admitted in the pleadings, but the court in its opinion stated that Piney Creek was a tributary of Sage Creek (Tr. 94) and that the defendants were enjoined from taking water from Piney Creek to the prejudice of the rights of Howell (Tr. 96). This decision was thereafter appealed and affirmed by the Circuit Court of Appeals, 86 C. C. A. 519, 159 Fed. 651, and by the United States Supreme Court, 221 U. S. 485, 55 L. Ed. 821.

This Federal Court decree of 1906 did not decree the rights of the defendants among themselves so thereafter

in 1907 in a suit in the District Court of Carbon County, State of Montana, the rights of the defendants as between themselves in the waters of Piney Creek was adjudicated (Tr. 120-125). Neither B. P. Loyning nor his predecessors in interest were parties to that suit.

Thereafter in 1919 predecessors in interest of B. P. Loyning moved the Howell point of diversion from Sage Creek in Wyoming upstream 15 miles to a point in Montana where water was taken from Piney Creek. Contempt proceedings were then instituted in 1919 in Federal Court in this cause No. 666 by predecessors in interest of B. P. Loyning against predecessors in interest of Helmet P. Loyning, and Judge Bourquin, who presided in this contempt matter, found the defendant guilty of contempt for interfering with complainants' prior rights, and found that the above change of diversion was a benefit to defendant (Tr. 104-112).

"At the times complained of the use of Howell's right on complainants' lands obviously required less of the natural flow than when used on Howell's lands some 15 miles farther down stream. Hence the change did not injure but benefitted respondents." (Tr. 109.)

This change in point of diversion was prior to that contempt proceeding.

Thereafter, in 1939, Helmet P. Loyning and a predecessor in interest of John Zweimer brought suit in the District Court of Carbon County, State of Montana, against B. P. Loyning seeking an adjudication that B. P. Loyning had no rights in the waters of Piney Creek and

seeking to enjoin him from appropriating water from Piney Creek (Tr. 167-176). B. P. Loyning filed his answer in said action (Tr. 147-166) and asserted that Piney Creek was a tributary of Sage Creek (Tr. 151, 161), pleaded the Federal Court decree of 1906 giving him a prior right to the waters of Sage Creek and its tributaries (Tr. 151, 161), alleging that the state court was without jurisdiction in the matter (Tr. 158), admitting the change in point of diversion from Sage Creek in Wyoming to Piney Creek in Montana (Tr. 153, 163) and denying that such change in point of diversion injured the plaintiffs (Tr. 154, 164). Plaintiffs in their reply (Tr. 136-146) denied that Piney Creek was a tributary of Sage Creek (Tr. 137, 143) and alleged that plaintiffs were damaged by the change in point of diversion (Tr. 140, 145). The state court found that Piney Creek was not a tributary of Sage Creek (Tr. 131, 132) contrary to the Federal Court decree of 1906, found that the change in point of diversion damaged the plaintiffs (Tr. 131-132), contrary to the findings of the Federal Court in the contempt decree of 1919, and found that plaintiffs' rights in Piney Creek were superior to defendant's and perpetually enjoined B. P. Loyning from taking water from Piney Creek to the detriment of plaintiffs (Tr. 133-134). On appeal to the Supreme Court of the State of Montana the judgment was affirmed (Tr. 178-207) on January 8, 1946, the court declining to pass on the question whether the Federal Court decree of 1906 was *res judicata* that Piney Creek was a tributary of Sage Creek (Tr. 197).



Thereafter, in the middle of June, 1946, Helmet P. Loyning and John Zweimer objected to B. P. Loyning taking any water from Piney Creek (Tr. 114). B. P. Loyning demanded of both Helmet P. Loyning and John Zweimer that they allow him to take water from Piney Creek to supply his rights under the Federal Court decree of 1906, but they refused (Tr. 114, 247), relying on the opinion of the Supreme Court of Montana (Tr. 215, 247).

B. P. Loyning then on July 11, 1946, instituted this contempt proceeding charging Helmet P. Loyning and John Zweimer with violating the Federal Court decree of 1906 (Tr. 3-10).

Helmet P. Loyning and John Zweimer filed separate answers (Tr. 12-22, 23-25), wherein they alleged that Piney Creek was not a tributary of Sage Creek, that they were damaged by the change in point of diversion, and pleaded the State Court decree as a defense to the action.

B. P. Loyning filed separate replies to these answers denying that Piney Creek was not a tributary of Sage Creek, denying that appellants were damaged by the change in point of diversion and alleging that the State Court decree was void since that court had no power or jurisdiction to review, vacate or annul the Federal Court decree of 1906 (Tr. 25-30).

The Court, the Honorable Charles N. Pray presiding, found all issues in favor of the appellee and adjudged appellants to be in contempt (Tr. 272-283).

This is an appeal by the appellants from that judgment.

## QUESTIONS INVOLVED

1. Whether or not the state court decree is a defense to this action?
2. If not, then whether or not Piney Creek is a tributary of Sage Creek and whether or not the change in point of diversion of the Howell right from Sage Creek to Piney Creek injured the appellants?
3. Whether or not the assertion of rights in conflict with a court injunction constitutes a contempt?

## SUMMARY OF ARGUMENT

When a judgment of another court is relied upon as a defense to an action, the court may inquire into the jurisdiction of such court rendering such judgment. The state court judgment was void since a state court has no power to review, modify or annul a prior Federal Court decree. The suit in Federal Court in 1906 was an action in rem to adjudicate water rights. The Federal Court in such actions retains jurisdiction to enforce its decrees to the exclusion of any other court. The state court had no power to interfere with the jurisdiction of the Federal Court first acquired and its decree was therefore void and no defense to this action.

A change of conditions may be a defense to a contempt proceeding, but the burden of proving a change of conditions is upon the parties who rely thereon. The evidence discloses that Piney Creek is a tributary of Sage Creek and there is no evidence that appellants were in-

jured by the change in point of diversion from Sage Creek to Piney Creek. The mere fact that a point of diversion is changed from the main stream to a tributary of such stream does not amount to injury per se to junior appropriators from the tributary.

The appellants, by asserting prior rights in the waters of Piney Creek under the state decree, violated the Federal Court injunction of 1906. Their actions as effectively deprived appellee of water as would have been the case if they had blocked off appellee's point of diversion or diverted all of the water above appellee's point of diversion. Appellee could not safely divert the water in the face of appellants' refusal, for fear of being in contempt of the state court decree.

## ARGUMENT

### *1. The State Court Decree of 1944 Is Void for Want of Jurisdiction and Is No Defense to This Proceeding.*

The state court decree of 1944 (Tr. 127-135) found that Piney Creek was not a tributary of Sage Creek (Tr. 131-132), and that the change in point of diversion from Sage Creek to Piney Creek damaged the appellants (Tr. 131-132) and held that the appellants' had prior rights in Piney Creek to those of appellee (Tr. 133-134). Appellants rely on this decree as a defense to this proceeding.

It is a well recognized rule of law that when a judgment of one court is offered as a defense to an action in another court, the latter court may inquire into the jurisdiction of the former over the parties or subject matter.

“When a judgment recovered in a state court is offered as a cause of action or as a defense in a federal court, the latter court may inquire into the jurisdiction of the former; and the effect of the judgment will be avoided if it is shown that the court rendering it lacked jurisdiction of the parties or of the subject matter. The rule is applicable even when the question is raised in a federal court sitting in the same state.”

34 C. J. 1159.

Cooper v. Brazelton, 135 Fed. 476, 479.

In re Philadelphia Rapid Transit Co., 117 Fed. (2d) 730, 733.

Clearly this court may inquire as to the jurisdiction of the state court over the subject matter of the action relied upon by appellants as a defense to this proceeding.

The decree of the state court is in direct conflict with the Federal Court decree of 1906 perpetually enjoining appellants' predecessors in interest from interfering with the Howell right to “the waters of Sage Creek and its tributaries” (Tr. 89). The findings of the state court were directly opposed to the opinion of Judge Whitson declaring that Piney Creek was a tributary of Sage Creek (Tr. 94, 96) and to the admission of appellants' predecessors (Tr. 63, 64, 65-66, 68, 70, 71, 101) that Piney Creek was a tributary of Sage Creek. The finding of the state court that the change in point of diversion injured appellants is directly opposed to the findings of Judge Bourquin in the contempt proceeding of 1919 (Tr. 109). Appellee in the state court challenged the jurisdiction of the state court (Tr. 158), but the latter chose to ignore



the prior jurisdiction of the Federal Court over the subject matter of the action.

It is well recognized that a state court has no jurisdiction to review, modify or annul the judgments or decrees of a Federal Court. Rather, an action to review a judgment can be brought only in the court which rendered the judgment.

“While a state court cannot ordinarily review, annul, or modify the judgments or decrees of a federal court, or interfere with the execution thereof, it may grant relief where there has been fraud on the federal court in procuring the judgment.”

21 C. J. S. 832.

“nor can a decree of a federal court be reviewed, annulled, or corrected by a state court, but application should be made to the court which has rendered such decree.”

15 C. J. 1176.

“An action to review a judgment can be brought only in the court which rendered the judgment.”

34 C. J. 404.

See also:

In re Rochester Sanitarium & Baths Co., 222 Fed. 22, 26.

Whayne v. McBirney, (Okl.) 157 P. (2d) 161, 163.

Fidler v. Gilchrist, (Ind.) 109 N. E. 796.

Kurtz v. Phila. & R. R. Co., (Pa.) 40 A. 988.

Gulf M. & N. R. Co. v. Hill Mfg. Co., (Miss.) 90 So. 358.



The suit in the state court was similar to a bill of review which is an old equity proceeding by which a party may obtain a review and reversal or correction of a decree of a court after it has become final.

30 C. J. S. 1049.

19 Am. Jur. 290.

New matter is one of the grounds recognized for such a bill of review.

30 C. J. S. 1069.

19 Am. Jur. 294.

Appellants, in instituting the action in state court were in effect seeking a bill of review of the Federal Court decree of 1906 and were relying on the change in point of diversion as new matter justifying a modification of that decree. But a state court has no jurisdiction of a bill to review a Federal Court decree. A bill of review can only be filed in the court which rendered the decree sought to be reviewed.

“The remedy afforded by bill of review is confined to courts of equity. Moreover, such a bill may not be entertained by a court other than that which rendered the decree sought to be reviewed.”

19 Am. Jur. 292.

“A federal court has jurisdiction of a bill of review if it had jurisdiction of the original cause; but it has no power thus to review a decision of a state court.”

30 C. J. S. 1054.

See also:

Nelson v. Bailey, (Mass.) 22 N. E. (2d) 116, 119.  
 People v. Sterling, (Ill.) 192 N. E. 229.

Furthermore, the suit in Federal Court in 1906 was an action in rem, similar to a suit to quiet title.

Whitcomb v. Murphy, 94 Mont. 562, 566, 23 Pac. (2d) 980 and cases cited therein.

State ex rel. Reeder v. Dist. Ct., 100 Mont. 376, 380, 47 Pac. (2d) 653.

Sain v. Montana Power Co., 20 F. Supp. 843.

In the last cited case it is said:

“In brief consideration of water rights and suits to adjudicate them, a water right and its exercise are hereditaments, corporeal and incorporeal. *Smith v. Denniff*, 24 Mont. 20, 25, 60 P. 398, 50 L. R. A. 737, 81 Am. St. Rep. 408. They are real property. *Adamson’s Case* (*Adamson v. Black Rock Power & Irrigation Co.*), 12 F. (2d) 437 (C. C. A.). Suits to adjudicate them are to quiet title to realty. *Rickey Land & Cattle Co. v. Miller & Lux* (C. C. A.) 152 F. 11, 15, affirmed 218 U. S. 258, 31 S. Ct. 11, 54 L. Ed. 1032. *Such suits are not in personam but in rem or quasi in rem*, for that, though directed against defendants personally, the real object is to deal with and settle and protect title to and enjoyment of particular property, and to invalidate unfounded claims asserted thereto. And that converts actions otherwise in personam into actions in rem or quasi in rem. See 1 C. J. 929 and cases; 51 C. J. 141, 281 and cases; *Pennoyer v. Neff*, 95 U. S. 714, 734, 24 L. Ed. 565.” *Italics ours.*)

The Federal Court, having rendered a final decree in 1906 permanently enjoining appellants from diverting waters of Piney Creek to the injury of appellee, retains jurisdiction to open, vacate or modify that decree upon a showing of facts making it equitable to do so.

43 C. J. S. 956, Section 218.

Only the court decreeing this permanent injunction has the power to open, vacate or modify it, it being well recognized that the court which first acquires jurisdiction of a suit in rem may maintain and exercise it to the exclusion of any other court until it has finally and completely disposed of the matter, and another court may not so exercise its jurisdiction as to frustrate or interfere with the jurisdiction first acquired.

“In *Baltimore & O. R. Co. v. Wabash R. Co.*, 57 C. C. A. 322, 119 Fed. 680, the circuit court of appeals for the seventh circuit said:

“It is settled that when a state court and a court of the United States may each take jurisdiction of a matter, the tribunal whose jurisdiction first attaches holds it, to the exclusion of the other, until its duty is fully performed, and the jurisdiction involved is exhausted, . . . . The rule is not only one of comity, to prevent unseemly conflicts between courts whose jurisdiction embraces the same subject and persons, but between state courts and those of the United States it is something more. “It is a principle of right and law, and therefore of necessity. It leaves nothing to discretion or mere convenience.” *Covell v. Heyman*, 111 U. S. 176, 28 L. Ed. 390, 4 Sup. Ct. Rep. 355. The rule is not limited to cases where property has actually been seized under judicial pro-

cess before a second suit is instituted in another court, but it applies as well where suits are brought to enforce liens against specific property, to marshal assets, administer trusts, or liquidate insolvent estates, and in all suits of a like nature. *Farmers' Loan & T. Co. v. Lake Street Elev. R. Co.*, 177 U. S. 51, 44 L. Ed. 667, 20 Sup. Ct. Rep. 564; *Merritt v. American Steel Barge Co.*, 24 C. C. A. 530, 49 U. S. App. 85, 79 Fed. 228.' "

*Kline v. Burke Construction Co.*, 260 U. S. 226, 67 L. Ed. 226, 230-231, 43 S. Ct. 79.

See also, to the same effect,

*Princess Lida v. Thompson*, 305 U. S. 456, 59 S. Ct. 275, 83 L. Ed. 285.

*Black Panther Oil & Gas Co. v. Swift*, (Okl.) 170 Pac. 238.

Consequently the state court has no power to assume jurisdiction in this matter. A suit to adjudicate water rights is in rem and where a perpetual injunction is issued the court so decreeing retains jurisdiction over the matter to modify or annul said decree if conditions so warrant. The state court had no power to assume jurisdiction in this matter so as to interfere with and frustrate the continuing jurisdiction of the Federal Court which was first acquired in this in rem proceeding.

The principles above set forth have been recognized and applied in water right suits. In *Rickey Land & C. Co. v. Miller & Lux*, 218 U. S. 258, 54 L. Ed. 1032, it was held that a Federal Court in Nevada and a state court in California have concurrent jurisdiction to determine the relative rights of parties claiming, one in Nevada and



one in California, to be entitled to appropriate, as against each other, the waters of an interstate stream, and whichever court first acquires jurisdiction is entitled to proceed to final determination without interference from the other. The court said:

“We are of the opinion, therefore, that there was concurrent jurisdiction in the two courts, and that the substantive issues in the Nevada and California suits were so far the same that the court first seised should proceed to the determination without interference, on the principles now well settled as between the courts of the United States and of the states. *Prout v. Starr*, 188 U. S. 537, 544, 47 L. ed. 584, 587, 23 Sup. Ct. Rep. 398; *Ex parte Young*, 209 U. S. 123, 161, 162, 52 L. ed. 714, 730, 13 L. R. A. (N.S.) 932, 28 Sup. Ct. Rep. 441.”

These rules have also been applied in water right suits as between different courts of the same state. The same rules as to priority and retention of jurisdiction apply as between courts of the same state (21 C. J. S. 745) as apply as between state courts and federal courts (21 C. J. S. 808). In *Consolidated H. S. Ditch & R. Co. v. New Loveland & G. Irr. & L. Co.*, (Colo.) 62 Pac. 364, suit was brought in the District Court of Boulder County to enjoin an interference with plaintiff's priority to the use of water as established by an earlier decree of that court. The defendant pleaded as a defense a subsequent judgment in his favor rendered by the District Court of Larimer County. The court held that the latter judgment was void.



“ . . . we are of opinion that since it is conceded, and appears of record, that the district court of Boulder County properly obtained jurisdiction of the proceedings which culminated in the decree of 1883, the district court of Larimer county did not, in the action which is relied upon in the fourth defense, have the power to review the decree of the district court of Boulder county, and that its attempt so to do was wholly without jurisdiction, and its judgment therein void. It follows from the foregoing that the judgment below should be affirmed; and it is so ordered. Affirmed.”

In *Weiland v. Reorganized Catlin Consol. Canal Co.*, (Colo.) 156 Pac. 596, an action was brought in the District Court of Otero County seeking to enjoin the water commissioners from distributing water otherwise than as adjudicated in an earlier case by the District Court of Bent County. The court held that only the court which originally adjudicated the water rights had jurisdiction in the matter.

“Which court is vested with authority to determine this question?

“If the district court of Otero county had jurisdiction for this purpose, it must, as it did, construe the decree of the Bent county district court, and do, as it did, render judgment directing the water officials to distribute the priority fixed by that decree in harmony with such constructions. Whether such construction and judgment are right or wrong is immaterial. The question is: When a court vested with jurisdiction to adjudicate water rights has exercised that authority and entered a decree, can another court of co-ordinate jurisdiction entertain a case the

object of which is to determine whether the water officials have complied with its terms in the distribution of water? The statutes designate the district court vested with exclusive jurisdiction to adjudicate priorities to the use of water for irrigation in a water district. When jurisdiction for that purpose has attached and a decree is entered, the statutes on that subject necessarily inhibit any other court of co-ordinate jurisdiction from modifying, reviewing, or construing such decree, otherwise there could be, in effect, more than one decree by different courts affecting the same priority to the use of water in the same water district, which it is the object of the statutes to avoid. \* \* \* \* \* *The enforcement of a decree establishing a priority to the use of water is of the very essence of adjudication proceedings. From its nature and object the process of enforcing it is continuous, and must therefore remain the continuing function of the court entering it.* Consequently, if a question arises between the owner of a priority fixed by a decree and water officials charged with the duty of distributing water under it, with respect to its meaning or effect, it must be determined by the court entering the decree, and not by any other court of co-ordinate jurisdiction.

“To conclude that any other court than the original one could entertain jurisdiction in such circumstances would lead to hopeless confusion and conflict in jurisdiction. \* \* \* Aside from this, the general rule applicable is that when a court assumes jurisdiction of a proceeding, which it is authorized to entertain, its jurisdiction is exclusive and extends to the enforcement of its decree in so far as the authority of other courts of the same jurisdiction may be involved. *Louden Canal Co. v. Haney Ditch Co.,*

supra; Bailey on Jurisdiction, § 77; Works on Courts and Their Jurisdiction, 69. We therefore conclude that the district court of Otero county was without jurisdiction to entertain the cause, and the demurrer to the complaint challenging its jurisdiction should have been sustained." (*Italics ours.*)

This decision is cited with approval or quoted from in the following cases:

El Paso & R. I. Ry. Co. v. Dist. Ct., (N. Mex.)  
8 Pac. (2d) 1064, 1067.

Bijou Irr. Co. v. Lower Latham Ditch Co., (Colo.)  
184 Pac. 292.

Farmers Ditch Co. v. Boyd Lake R. & I. Co.,  
(Colo.) 178 Pac. 561.

In Hazard v. Joseph W. Bowles Reservoir Co., (Colo.)  
287 Pac. 854, 855, it is said:

"The district court of Douglas county first acquired jurisdiction to adjudicate the relative priorities of right to the use of water for irrigation in this district, and it has entered its decree awarding to the parties in this action their relative priority rights to the use of water in this reservoir. No other district court in this state has the jurisdiction thereafter to adjudicate such matters. The district court of Douglas county, having first obtained jurisdiction to adjudicate priorities to the use of water for irrigation in that district, thereafter retains exclusive jurisdiction over the subject matter of such priorities."

\* \* \*

"It is too clear for argument that the district court of Arapahoe county, in rendering the decree in the action now before us, not only assumed to interpret

and construe and modify the decree of the district court of Douglas county, which was the only court that has jurisdiction in the premises, but, in effect, set it aside, nullified it, and absolutely deprived the defendants of the right to use any of the water, in any circumstances, impounded in the Bennet reservoir.

"The judgment of the district court is therefore set aside and held for naught."

See also *Louden Irrigating Canal Co. v. Handy Ditch Co.*, (Colo.) 43 Pac. 535.

The above cited cases are positive authority that the priority of water rights as between appellants and appellee having been first adjudicated by the Federal court in 1906, no other court thereafter has jurisdiction in an action concerning those adjudicated rights. If appellants contend that appellee's change in point of diversion prejudices their rights, that issue can be litigated only by the Federal Court which originally adjudicated those rights.

The only case found taking a contrary position and which appellants cite is *Sain v. Montana Power Co.*, 84 Fed. (2d) 126. That was an action commenced in the District Court of the United States for the District of Montana, Judge Bourquin presiding (the same Judge who presided in the contempt proceeding of 1919), seeking to enjoin the defendant from changing its point of diversion. The rights in the stream were originally adjudicated in the state court and Judge Bourquin held that he had no jurisdiction in the matter by reason of the prior and continuing jurisdiction of the state court (*Sain v. Mon-*



tana Power Co., 5 F. Supp. 792). The judgment was reversed on appeal to this court, the court pointing out that in Montana, after water rights have been adjudicated, the parties may bring actions concerning such rights in actions distinct from the cause in which the rights were originally adjudicated. The cases of *State ex rel. Boston & Montana etc. Mining Co. v. Clancy*, 30 Mont. 193, 76 Pac. 10, *Mannix & Wilson v. Thrasher*, 95 Mont. 267, 26 Pac. (2d) 373, and *Thrasher v. Mannix & Wilson*, 95 Mont. 273, 26 Pac. (2d) 370 are cited. It is true that those cases recognize that after water rights have been adjudicated, suits distinct from the original action may be maintained, in the sense that distinct Cause Numbers are assigned to them. But that entirely begs the issue. The question is whether such subsequent actions may be tried in a different court from that in which the rights were originally adjudicated. In each of the cited cases the subsequent litigation was tried in the same court which had previously adjudicated the question, and according to the decisions heretofore cited, that is the procedure which must be followed. It is further submitted that the Court was in error in holding that the suit was in personam. The mere fact that injunctive relief is sought in an action to adjudicate water rights does not convert an action in rem into one in personam.

Thereafter the cited case (*Sain v. Montana Power Co.*) was heard by Judge Bourquin and dismissed since there was no showing of injury from the change in place of diversion. Judge Bourquin's entire opinion is devoted to an exhaustive criticism of the opinion of this court, and



we commend it to the consideration of the court (*Sain v. Montana Power Co.*, 20 F. Supp. 843).

A subsequent opinion of the Montana Supreme Court, *State ex rel. Swanson v. Dist. Ct.*, 107 Mont. 203, 82 Pac. (2d) 779, shows clearly that once water rights have been adjudicated, subsequent actions dealing therewith, although distinct from the original action, must be commenced in the same court. In that case the District Court of Cascade County adjudicated water rights to streams flowing in Cascade, Teton and Lewis and Clark counties. Thereafter it was sought in the District Court of Lewis and Clark County to secure the appointment of a water commissioner to distribute waters under this decree. It was held that the latter court had no jurisdiction in the matter.

“Sun River and its tributaries flowing, as they do, in three counties, viz., Lewis and Clark, Teton and Cascade, the district court of any one of those counties has jurisdiction to adjudicate the water rights of the whole watershed system. (*Whitcomb v. Murphy*, 94 Mont. 562, 23 Pac. (2d) 980.) But of the three, the court which first acquired jurisdiction—here the district court of Cascade county—retains jurisdiction for the purpose of disposing of the whole controversy, and no court of co-ordinate power is at liberty to interfere with its action. (15 C. J. 1134.)

\* \* \*

“Counsel for relators contend that even though the district court of Cascade county be conceded to have exclusive jurisdiction to adjudicate the rights of all parties to the waters of Sun River and its tributaries, it does not follow that that court has exclusive

jurisdiction to enforce the decree. With this contention we do not agree."

The court then quoted at length from *Weiland v. Reorganized Catlin Con. Canal Co.*, (Colo.) 156 Pac. 596, herefore discussed and quoted in this brief.

It is submitted that the state court decree relied upon as a defense to this action is void. That court had no jurisdiction to interfere with the jurisdiction of the Federal Court first acquired, and to review and annul the Federal Court decree of 1906.

Even if the State court decree were valid, it would be no defense to this action. *De La Mater v. Graves*, (Colo.) 193 Pac. 552, is a case somewhat similar in principle. There it appeared that the plaintiff in error had obtained a divorce from the respondent in New Mexico, the decree providing that the plaintiff in error was to have custody of the minor children for one month. Plaintiff in error then sued in Colorado to enforce this decree and the Colorado court awarded the custody of the children to the plaintiff in error for 30 days, at the end of which time they were to be returned to the respondent. Plaintiff in error did not return the children to the respondent at the end of the 30 days and he was cited for contempt. He pleaded as a defense that the New Mexico decree had subsequently been modified, awarding the children to him unconditionally and absolutely. The court held that this was no defense to the contempt proceedings.

"Assuming that the second New Mexico decree was such as thus pleaded, and that it was proven in the contempt proceedings, the question to be deter-

mined is whether the plaintiff in error could rely upon such decree of a foreign state as a defense in these contempt proceedings.

"The order which the plaintiff in error disobeyed was that he could within 30 days return and deliver the minor children to their mother at Durango, Colo. This order he was bound to obey unless and until the court making it should vacate it in the meantime. No court in another state could affect that order. A foreign court could not expressly vacate or annul it. 15 C. J. 1184. It follows from this that no court of a sister state could affect an order of a court in this state by making some order in conflict, or rendering some decree inconsistent therewith. The order in question was valid when made, and valid when disobeyed, and the rendition of the second New Mexico decree affords no defense in this contempt proceeding.

"Assuming that the Colorado court was bound to give full force and effect to the New Mexico decree under the general rules of comity, it could not do so by simply regarding its own previous order or judgment as a nullity, since its jurisdiction could not be divested by anything done by a court of another state. The Colorado court might, however, vacate its order, but, until it does so, the order must be obeyed. If facts arise which would justify a vacation of the order, that is no excuse for disobeying the order. The remedy of the party desiring to be relieved from the necessity of obeying the order is to take formal and due steps in the proceeding in which the order was made, and not to impeach the order in contempt proceedings brought to punish a disobedience thereof. *State ex rel. Tuthill v. Giddings*, 98 Minn. 102, 107 N. W. 1048; 13 C. J. 44, § 59."

Here the appellants are relying on a decree of a state court to justify their disobedience of the Federal Court decree of 1906. But the state court decree is void. The decree of the Federal Court is still in force and the state court decision cannot affect it or justify appellants in disobeying it. Appellants are bound to obey the Federal Court decree until such time as it is modified or vacated in a proper proceeding before that court.

2. *Appellants Failed to Show a Change of Conditions Justifying Their Violation of the Federal Court Decree.*

Appellants argue at page 36 of their brief that the only burden on them was to show that the issues decided by the state court in 1944 were the same as the issues in this proceeding, and having established that fact, the state court decree is res judicata and purges them of contempt. Whether that be true or not (*De La Mater v. Graves*, (Colo.) 193 Pac. 552 (*supra*) holds that it is not) need not be decided, since, as heretofore shown, the state court decree was void and of no effect for any purpose. If it be contended that conditions have changed since 1906, justifying a disobedience of the Federal Court decree, the burden is upon appellants to show such a change in conditions.

17 C. J. S. 111.

*National Labor Relations Board v. Fed. Bearings Co.*, 109 Fed. (2d) 945.

The burden of proving an injury by the change in point of diversion, if there was an injury, was upon appellants.



Thrasher v. Mannix & Wilson, 95 Mont. 273, 26 Pac. (2d) 370.

Jacob v. Lorenz, (Cal.) 33 Pac. 119.

Appellants introduced some evidence tending to show that Piney Creek was not a tributary of Sage Creek, and that if it was it did not make any beneficial contribution to Sage Creek. Such testimony was controverted by appellee and the trial court found in appellee's favor on these points. Apparently appellants admit that their evidence was insufficient in that connection as they claim no error therein.

Appellants also contended in the lower court that appellee, by changing his point of diversion from the main stream to only one tributary of that stream, ipso facto lost the whole of his prior right. Apparently appellants are now satisfied that they were in error in that connection since they make no such contention before this Court.

It is of course well recognized that an appropriator may, without losing his priority, change his point of diversion if the rights of others will not be materially injured or prejudiced. Changing the point of diversion upstream often benefits junior intervening appropriators due to the savings of water which would otherwise be lost by reason of evaporation, sinking, seepage, etc.

Ironstone Ditch Co. v. Ashenfelter, (Colo.) 140 Pac. 177, 182.

Crippen v. Glasgow, (Colo.) 87 Pac. 1073.

The same rules are applicable where the point of diversion is changed to a tributary of the main stream.



Spring Creek Irr. Co. v. Zollinger, (Utah) 197  
Pac. 737.

The prior right is not lost unless junior appropriators are prejudiced. And there is absolutely no evidence in this case that the appellants were prejudiced. Judge Bourquin in the contempt proceedings of 1919 found that this change in point of diversion benefitted the appellants (Tr. 109) and there is no evidence that conditions have changed since that time. Appellants offered no evidence to show that there was any natural flow of water at the old point of diversion in Wyoming. There was none at the time of the contempt proceedings in 1919 (Tr. 106). If the point of diversion had not been changed the appellants would have been required to allow sufficient water to pass down Piney Creek to satisfy appellee's rights, which would be something over 110 inches, because of evaporation and sinkage. The move upstream, therefore, in the absence of a showing that there was now a natural flow of water at the old point of diversion, benefitted rather than prejudiced appellants.

The appellants wholly failed to sustain their burden of proof to show facts excusing their violation of the Federal Court injunction of 1906.

### *3. Appellee Proved the Charge of Contempt*

The evidence discloses that about the middle of June, 1946, the appellants objected to appellee diverting any water from Piney Creek (Tr. 114); that appellee then demanded of appellants that they allow him to use the

water, but that they refused, relying on the state court decree (Tr. 114, 215, 247); and that as a result of being thus deprived of water appellee's crops were damaged (Tr. 114).

Appellants argue that since their points of diversion were below that of appellee, their verbal refusal to allow appellee to take any water, unaccompanied by affirmative acts, does not constitute contempt. Appellee is not able to agree with that contention and appellants cite no authority in support of their position. It is appellee's contention that appellants' verbal assertion of rights hostile to the Federal Court decree of 1906 was in contempt of that decree. It is to be noted that had appellee disregarded appellants' refusal he would have been running the risk of being cited for contempt of the state court decree. Under the circumstances appellants' refusal was just as effective as if they had blocked appellee's headgate or diverted all of the water above appellee's point of diversion.

To employ a subterfuge to evade a court decree constitutes a contempt (12 Am. Jur. 406). The state court decree constituted that subterfuge and the assertion of rights under that decree in hostility to the Federal Court decree and in direct violation thereof constituted a contempt of the latter.

It is to be further noted that the Federal decree of 1906 perpetually enjoined the appellants from "*in any manner interfering with the rights*" of the senior appropriator. (Tr. 89.) Certainly the acts of appellants were in contempt of that decree. The mere fact that appellants' points of diversion were downstream from appellee does not

permit them to flaunt the state court decree in direct violation of appellee's rights under the Federal Court decree.

## CONCLUSION

The state court decree is void and no defense to this action since the water rights as between the parties were originally adjudicated in the Federal Court wherein appellants were perpetually enjoined from interfering with appellee's prior rights. The Federal Court retains jurisdiction in such a case to enforce its decree and no other court has jurisdiction to review, modify or annul that injunction.

Appellants violated the injunction of the Federal Court by asserting rights in violation thereof and refusing to allow appellee to divert the water to which he was entitled.

No change in conditions or excusatory facts were proved by appellants.

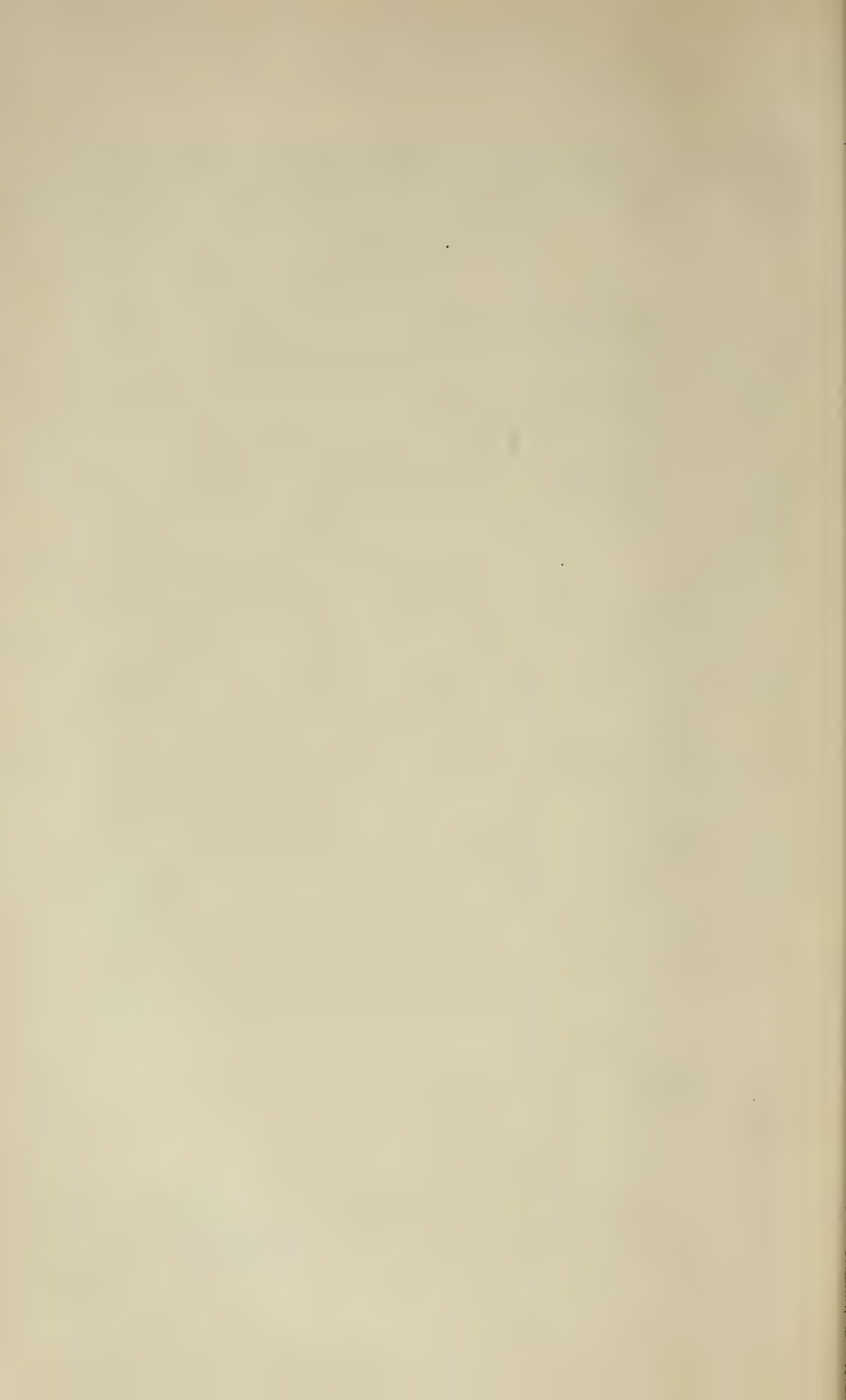
Appellee has endeavored not to unduly extend this brief. The question involved are fully considered in the opinion of the court (Tr. 272-283) and the question as to the jurisdiction of the state court is discussed at length by Judge Bourquin in *Sain v. Montana Power Co.*, 20 F. Supp. 843, to which opinions the attention of the Court is invited.

The judgment must be affirmed.

Respectfully submitted,

RALPH J. ANDERSON

*Attorney for Appellee  
and Petitioner*



No. 11218

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**United States**  
**Circuit Court of Appeals**  
**For the Ninth Circuit**

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HELMET P. LOYNING and JOHN ZWEIMER,  
*Respondents and Appellants,*

*vs.*

B. P. LOYNING,

*Petitioner and Appellee.*

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**PETITION FOR REHEARING**

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**FILED**

JAN 25 1949

**PAUL P. O'BRIEN,**  
**CLERK**

**RALPH J. ANDERSON**

*Attorney for Appellee  
and Petitioner*





**United States**  
**Circuit Court of Appeals**  
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HELMET P. LOYNING and JOHN ZWEIMER,  
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---

**PETITION FOR REHEARING**

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*To the United States Court of Appeals for the Ninth  
Circuit, and the Judges Thereof:*

Comes now B. P. Loyning, the appellee in the above-entitled cause, and presents this, his petition for a rehearing of the above entitled cause, and, in support thereof, respectfully shows:

I.

That the decision of the above-entitled Court is based upon a misapprehension of the law in that the Court states that there must be a violation of the "letter and spirit" of the Federal Court decree to constitute a contempt, whereas the law is that the violation of the spirit of an injunction,

even though its strict letter may not have been disregarded, is a breach of the mandate of the Court.

- Pfeiffenberger v. Illinois Terminal R. Co., (Ill.) 69 N. E. (2d) 355;  
 Securities and Exchange Commission v. Okin, 2 Cir., 137 F. (2d) 862, and cases cited therein;  
 John B. Stetson Co. v. Stephen L. Stetson Co., 2 Cir., 128 F. (2d) 981, and cases and authorities therein cited;  
 Ginsberg v. Kentucky Utilities Co., (Ky.) 83 S. W. (2d) 497, and cases therein cited;  
 State v. Freshwater, (W. V.) 148 S. E. 6, and authorities therein cited;  
 Rapalje on Contempt, Section 40;  
 43 C. J. S., Injunctions, Section 264 a, p. 1016, note 71.

## II.

That the opinion of the Court disregards the well established rule that no scheme or subterfuge, however artfully designed to disguise its real nature and purpose, will be allowed to succeed if it constitutes in effect a substantial violation of the injunction.

- 43 C. J. S., Injunctions, Section 264 a, p. 1016, note 73;  
 Southwestern Loan & Fin. Corp. v. Arkansas Transp. Co., (Ark.) 45 S. W. (2d) 501, and cases therein cited;  
 Ginsberg v. Kentucky Utilities Co., (Ky.) 83 S. W. (2d) 497, and cases therein cited.

## III.

That the Court is in error in holding that the fact that lawyers hold "entirely opposite views as to which decree controls" will excuse a contempt of the Federal Court decree. Advice of counsel is no defense to a proceeding for contempt. It may only be considered in mitigation of the offense.

17 C. J. S., Contempt, Section 38.

## IV.

That the decision of the Court is contrary to the evidence. The Court recognizes that had the appellee diverted the water, which appellants refused to allow him to take under the Federal decree, the appellants might have "instituted contempt charges under the state decree." The action of the appellants in re-litigating the priority of these water rights in the state court and in asserting the priority of the state decree over the Federal decree and in refusing to allow appellee to divert water under the federal decree, constituted the subterfuge which violated the spirit of the Federal decree and placed appellants in contempt thereof. Appellants' action and conduct as effectively deprived appellee of the water to which he was entitled under the Federal decree as would have been the case had they dammed up his headgate or diverted all the water before it reached his headgate. By this scheme and subterfuge appellants effectively circumvented the Federal decree. The spirit of that decree has been violated, and under the authorities cited in paragraphs I and II above, appellants are in contempt. The Federal decree enjoined appellants

from "in any manner interfering with" appellee's prior rights, and appellants' actions violated that decree.

WHEREFORE, upon the foregoing grounds, it is respectfully urged that this petition for a rehearing be granted and that the judgment of the District Court of the United States in and for the District of Montana be upon further consideration affirmed.

Respectfully submitted,

RALPH J. ANDERSON  
*Attorney for Appellee*

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### CERTIFICATE

I, Ralph J. Anderson, do hereby certify that I am the counsel for B. P. Loyning, the appellee in the above-entitled action, and that the foregoing petition for rehearing is not interposed for purposes of delay, but is presented in good faith and in my judgment is well founded and proper to be filed herein.

RALPH J. ANDERSON





